Supreme Court, U.S.
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In The

Supreme Court of the United States

DAVID A. GILL, CHAPTER 7 TRUSTEE,

Petitioner,

v.

STEVEN H. STERN,

Respondent.

On Petition For A Writ Of Certiorari To The United States Court Of Appeals For The Ninth Circuit

PETITION FOR A WRIT OF CERTIORARI

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QUESTION PRESENTED

This case arises in a bankruptcy case as part of a bankruptcy trustee's attempt to exercise his statutory avoidance power for the benefit of creditors to recover massive pre-bankrutpcy transfers. It presents this Court with an opportunity to clarify the intersection of fraudulent transfer law and exemption planning law that has created confusion and uncertainty in the lower federal courts. The decision of the Ninth Circuit Court of Appeals below provides substantial, perhaps unlimited opportunities for debtors to shelter their assets from trustees and creditors and may well create an ironclad rule insulating debtors from the recovery efforts of trustees. The decision of the Ninth Circuit Court of Appeals has created a conflict among the circuits. This makes for great uncertainty as trustees attempt to exercise their statutory powers and as counsel seek to provide guidance to clients seeking to plan their financial matters.

More fully, the first issue in this case is whether a pre-petition transfer by the debtor of $1.4 million from an IRA account to a newly formed ERISA-qualified pension plan ("Plan") is unavoidable as a matter of law. The transfer moved cash from an account that creditors could reach to one they could not. The transfer occurred in conjunction with other transfers of over $2,000,000 in property interests and a divorce within weeks of the issuance of a $4,585,000 arbitration award against the debtor, all pre-petition.

The second issue in the case arises from the related summary conclusion that the Plan established under those circumstances was exempt from the debtor's bankruptcy estate as a private retirement plan and that the alleged fraudulent transfer did not void the claimed exemption.

QUESTION PRESENTED – Continued

Thus, Petitioner respectfully requests that certiorari be granted on the following question:

Can a bankruptcy debtor be determined as a matter of law to have only engaged in permissible exemption planning, and his exemption be sustained, when the record presents evidence of fraudulent intent in the making of the questioned pre-petition transfer?

PARTIES TO THE PROCEEDING

Petitioner, David A. Gill, is the Chapter 7 Trustee for the bankruptcy estate of Steven H. Stern, debtor.

Steven H. Stern, the debtor/respondent herein, was the appellee below. Stern also was an appellant below seeking review of a determination by the District Court that the Plan was not excluded from the bankruptcy estate because, as of the petition date, there was no covered employee, Stern having married his former employee by that time. That determination was affirmed by the Ninth Circuit and is not the subject of this Petition.

TABLE OF CONTENTS

	Page
QUESTION PRESENTED	i
PARTIES TO THE PROCEEDING	iii
PETITION FOR A WRIT OF CERTIORARI	1
OPINIONS BELOW	1
JURISDICTION	1
STATUTES INVOKED	1
STATEMENT OF THE CASE	4
A. The Fraudulent Transfer	4
B. The Plan Exclusion/Exemption Issue	7
COURT OF APPEALS' DECISION	8
ARGUMENT	9
CONCLUSION	13

TABLE OF AUTHORITIES

Page

CASES

Grogan v. Garner, 498 U.S. 279 (1991) 9

In re Lapes, 254 B.R. 501 (Bk. SD Florida 2000) 12

Reading Company v. Brown, 391 U.S. 471 (1968) 13

Segal v. Rochelle, 382 U.S. 375 (1966) 13

In re Sholdan, 217 F.3d 1006 (8th Cir. 2000) 9, 10, 12

Tavenner v. Smoot, 257 F.3d 401 (4th Cir. 2001), *cert. denied*, 534 U.S. 1116 (2002) 10, 11

In re Wadley, 263 B.R. 857 (Bk. SD Ohio 2001) 11, 12

Yates v. Henton, 123 S.Ct. 2637 (2003) 8

STATUTES

28 U.S.C. § 1254(1) 1

California Civil Code § 3439.04 1

California Civil Code § 3439.04(a) 2

California Civil Code § 3439.04(b) 2

California Civil Code § 3439.04(b)(1) 6

California Civil Code § 3439.04(b)(2) 6

California Civil Code § 3439.05 ..... 2, 6

California Code of Civil Procedure § 704.115(a) 2

California Code of Civil Procedure § 704.115(b) 2

California Code of Civil Procedure § 704.115(d) 2

California Code of Civil Procedure § 704.115(e) 2

PETITION FOR A WRIT OF CERTIORARI

Petitioner David A. Gill, Chapter 7 Trustee ("Trustee") for the estate of Steven H. Stern, debtor ("Stern") respectfully petitions for a writ of certiorari to review an Order and Amended Opinion of the United States Court of Appeals for the Ninth Circuit (the "Court of Appeals").

OPINIONS BELOW

The Order and Amended Opinion ("Amended Opinion") of the Court of Appeals [Appendix: 1-25] is reported at 345 F.3d 1036. That Amended Opinion amended and superseded a prior Opinion of the Court of Appeals reported at 317 F.3d 1111 [Appendix: 26-45].

JURISDICTION

The initial Opinion of the Court of Appeals was filed February 4, 2003. The Trustee filed a timely petition for panel rehearing and/or rehearing en banc on February 12, 2003 ("Petition for Rehearing"). The Court of Appeals filed its Amended Opinion on October 7, 2003. This Court's jurisdiction is invoked under 28 U.S.C. § 1254(1).

STATUTES INVOKED

The statutes principally involved in this case are:

1) California Civil Code § 3439.04, which reads as follows:

> A transfer made or obligation incurred by a debtor is fraudulent as to a creditor, whether the creditor's claim arose before or after the transfer was made or the obligation was incurred, if the debtor made the transfer or incurred the obligation as follows:
>
> (a) With actual intent to hinder, delay, or defraud any creditor of the debtor.
>
> (b) Without receiving a reasonably equivalent value in exchange for the transfer or obligation, and the debtor:
>
> (1) Was engaged or was about to engage in a business or a transaction for which the remaining assets of the debtor were unreasonably small in relation to the business or transaction; or
>
> (2) Intended to incur, or believed or reasonably should have believed that he or she would incur, debts beyond his or her ability to pay as they became due.

2) California Civil Code § 3439.05, which reads as follows:

> A transfer made or obligation incurred by a debtor is fraudulent as to a creditor whose claim arose before the transfer was made or the obligation was incurred if the debtor made the transfer or incurred the obligation without receiving a reasonably equivalent value in exchange for the transfer or obligation and the debtor was insolvent at that time or the debtor became insolvent as a result of the transfer or obligation.

3) California Code of Civil Procedure § 704.115(a), (b), (d) and (e), which read as follows:

(a) As used in this section, "private retirement plan" means:

(1) Private retirement plans, including, but not limited to, union retirement plans.

(2) Profit sharing plans designed and used for retirement purposes.

(3) Self employed retirement plan, and individual retirement annuities or accounts provided for in the Internal Revenue Code of 1986, as amended, including individual retirement accounts qualified under Section 108 or 408A of that code, to the extent the amounts held in the plans, annuities, or accounts do not exceed the maximum amounts exempt from federal income taxation under that code.

(b) All amounts held, controlled, or in process of distribution by a private retirement plan, for the payment of benefits as an annuity, pension, retirement allowance, disability payment, or death benefit from a private retirement plan are exempt.

(d) After payment, the amounts described in subdivision (b) and all contributions and interest thereon returned to any member of a private retirement plan at, exempt.

(e) Notwithstanding subdivisions (b) and (d), except as provided in subdivision (f), the amounts described in paragraph (3) of subdivision (a) are exempt only to the extent necessary to provide for the support of the judgment debtor when the judgment debtor retires and for the support of the spouse and dependents of the judgment debtor, taking into account all resources that are likely to be available for the support of the

judgment debtor when the judgment debtor retires. In determining the amount to be exempt under this subdivision, the court shall allow the judgment debtor such additional amount as is necessary to pay any federal and state income taxes payable as a result of the applying of an amount describes in paragraph (3) of subdivision (a) to the satisfaction of the money judgment.

STATEMENT OF THE CASE

A. The Fraudulent Transfer.

Stern is a movie director who became embroiled in disputes with Dove Audio, Inc. ("Dove") and others over a particular project which led to arbitration proceedings.[1] In or about September 1992, he suffered an adverse arbitration award ("Arbitration Award") in the amount of $4,585,000.00 in favor of Dove. Stern then obtained an uncontested divorce in or about October 1992. He then also transferred property worth in excess of $2 million without the benefit of any property appraisals in that uncontested divorce. Moreover, he then transferred $1.4 million from his non-exempt IRA into a purportedly ERISA-qualified pension plan ("IRA Transfer") and transferred other assets to relatives. The Plan was established by Stern immediately after the Arbitration Award against him. When established, the Plan had one covered employee, Maggie Mayersohn ("Mayersohn"), whom Stern thereafter married.

[1] The facts are drawn from the majority and dissenting opinions in the Ninth Circuit's Amended Opinion.

In November, 1992, Stern filed an initial bankruptcy case, which he was allowed to dismiss. Thereafter, Dove commenced fraudulent transfer litigation against Stern in the California state courts. When Stern then commenced the present bankruptcy case in 1995, the Trustee intervened in the Dove fraudulent transfer action on behalf of all creditors of the estate and it was removed to the Bankruptcy Court. The fraudulent transfer adversary proceeding in the Bankruptcy Court challenged the marital dissolution transfers as well as the IRA Transfer.

The operative complaint in the adversary proceeding was the Trustee's Fourth Amended Complaint. [Appendix: 87-107] The general allegations described a series of events beginning in September of 1992, when Dove obtained the Arbitration Award for $4,585,000 against Stern and his various corporations. It was alleged that, in response to the Arbitration Award, Stern and others, beginning in or about October of 1992, undertook a series of calculated and fraudulent acts pursuant to which Stern transferred substantially all of his valuable, non-exempt assets in an attempt to place such assets beyond the reach of his then existing creditors, particularly Dove. It was alleged, for instance, that in the matter of a few days following the Arbitration Award, from October 13, 1992 through October 19, 1992, Stern transferred approximately $725,000 in cash (para. 18-21). It was further alleged that at that time he also transferred other cash and interests in various items of real property, as described above.

It was also alleged in the Complaint that in or about October of 1992, Stern transferred approximately $1,400,000 from a non-exempt personal IRA account to a purportedly

ERISA-qualified corporate pension plan ("the Plan") he had then just established ("the IRA Transfer").

Based on these allegations, several claims for relief were asserted. The First through Third Claims for Relief, which were against Stern's ex-wife and his daughter and son-in-law, dealt with the marital dissolution transfers, and are not at issue in the appeal.

The Fourth Claim for Relief was against Stern and the Plan and asserts that the IRA Transfer was made with the actual intent to hinder, delay or defraud creditors.

In the Complaint the Fifth Claim against Stern and the Plan again dealt with the IRA Transfer and alleged constructive fraud under the California version of the Uniform Fraudulent Transfer Act, California Civil Code § 3439.04(b)(1) and (2), i.e., while Stern was insolvent (para. 47), the transfer was made with a failure to receive reasonably equivalent value (para. 44) or made while assets were unreasonably small (para. 45), or made while debts would be incurred beyond the debtor's ability to pay (para. 46).

The Sixth Claim for Relief against Stern and the Plan asserted that the IRA Transfer was made at the time the Debtor was insolvent and for lack of reasonably equivalent value under California Civil Code § 3439.05 (paras. 50 and 51).

Stern moved the Bankruptcy Court in the fraudulent transfer adversary proceeding for partial summary judgment as to the claims for relief based on the IRA Transfer, asserting that those claims were appropriate for summary dismissal. The Bankruptcy Court held that summary judgment was appropriate because, without the need for a

trial on Stern's actual intent, it believed the IRA Transfer was immunized as a matter of law from attack as pre-bankruptcy exemption planning.

On August 25, 1998, the Bankruptcy Court entered its Judgment in favor of Stern, summarily dismissing the Fourth, Fifth, and Sixth Claims for Relief in the Fourth Amended Complaint and appeal to the District Court timely followed.

The District Court affirmed the Bankruptcy Court in an unpublished opinion, upholding the summary determination that the challenged IRA Transfer, as a matter of law, was permissible exemption planning [Appendix: 58-86]. The Ninth Circuit, by a 2-1 majority, affirmed.

B. The Plan Exclusion/Exemption Issue.

Stern also moved for summary judgment on the Plan exclusion and exemption from the bankruptcy estate. He was also granted summary judgment in his favor on that motion. While the Bankruptcy Court found the Plan to be both excluded from the estate and exempt, the District Court concluded that while the Plan was not excluded because, upon Stern's marriage to Mayersohn, the Plan lost its ERISA qualification, it was fully exempt. The Ninth Circuit, all judges concurring, agreed that the Plan was not excluded because, on the petition date there being no covered employee, the Plan was no longer ERISA qualified. The majority concluded it was nevertheless exempt and any fraudulent transfer would not void the exemption, sustaining the summary judgment. The

dissent found triable issues on the IRA Transfer and, thus, on the applicability of the exemption.[2]

COURT OF APPEALS' DECISION

The initial Opinion of the Court of Appeals filed February 4, 2003 affirmed the District Court by a 2-1 majority. The majority initially held that the Trustee's burden of proof at the time of trial for the fraudulent transfer claim was clear and convincing evidence and that such burden had not been met. It consequently affirmed the summary judgments against the Trustee on the fraudulent transfer and exemption issues. Senior Circuit Judge Alarcón concurred with the majority's conclusion that the Plan was not excluded from the bankruptcy estate because of the lack of a covered employee as of the petition date, but dissented from the decision to affirm the summary judgments, concluding that there was sufficient evidence in the record to make triable the issue of Stern's fraudulent intent and consequent loss of any exemption in the Plan.

The Trustee's Petition for Rehearing [Appendix: 46-57] focused on the assumption in the majority opinion that the Trustee's burden of proof at the time of trial was clear and convincing evidence. The Petition for Rehearing argued that the burden of proof, in fact, was a preponderance of

[2] In the case of *Yates v. Henton*, 123 S.Ct. 2637 (2003) this Court granted a petition for a writ of certiorari to review the issue of whether or not, if the debtor is one, but not all, of a plan's covered employees, a plan has lost its ERISA qualification.

the evidence and that conclusion flowed in part from this Court's decision in *Grogan v. Garner*, 498 U.S. 279 (1991). The Petition for Rehearing argued that a proper evaluation of the burden of proof should compel the majority to reach the same conclusion that the dissent did.

The Amended Opinion, under the force of *Grogan*, amended the prior Opinion on the burden of proof (adopting the preponderance standard) but concluded, nevertheless, that the summary judgment against the Trustee was proper. Judge Alarcón again dissented, finding that there were sufficient facts adduced to require a trial on Stern's actual fraudulent intent.

ARGUMENT

This Court should grant the Petition for Writ of Certiorari because the decision of the Ninth Circuit is contrary to recent decisions from other circuits that require an evidentiary assessment of extrinsic facts before a conclusion can be reached that a particular transfer was more than exemption planning and in fact fraudulent.

Of particular interest on this analysis of extrinsic facts are two recent decisions of other Courts of Appeals. In the case of *In re Sholdan*, 217 F.3d 1006 (8th Cir. 2000), the Eighth Circuit sustained a decision that the debtor, even though ninety years of age and afflicted with various medical problems and living pre-petition in an assisted care facility, had acted with fraudulent intent when, immediately pre-petition, he converted virtually all of his non-exempt assets into an exempt homestead. As the Eighth Circuit noted:

> On these facts, we find the bankruptcy court correctly concluded there was ample evidence extrinsic to the mere conversion of assets that showed fraudulent intent on the part of the debtor. It is one thing to convert non-exempt assets into exempt property for the express purpose of holding it as a homestead and thereby putting the property beyond the reach of creditors [Citation]. However, it is quite another thing to acquire title to a house for no other reason than to defraud creditors. *Sholdan*, *supra* at page 1010-1011.

It is interesting to note that Judge Arnold's dissent is expressly based on the notion of permissible exemption planning, *Sholdan*, *supra*, at page 1011-1012. The *Sholdan* court adopts the extrinsic fact analysis which underlies Judge Alarcón's dissent in the Amended Opinion.

Similarly, in *Tavenner v. Smoot*, 257 F.3d 401 (4th Cir. 2001), *cert. denied*, 534 U.S. 1116 (2002), the Fourth Circuit held that a bankruptcy trustee could avoid a transfer of potentially exempt property on the ground that the debtor transferred the property with the intent to hinder, delay, or defraud creditors. Rejecting the "no harm, no foul" approach to this question, the Fourth Circuit concluded that the "no harm, no foul" approach was inconsistent with the Bankruptcy Code, *Tavenner*, *supra*, at page 406-407. The court also rejected the argument that "transfers cannot be characterized as fraudulent because it is impossible to hinder, delay, or defraud creditors by transferring property to which the creditors were not entitled in the first place." *Tavenner*, *supra*, at page 407. Rejecting that argument squarely, the Fourth Circuit held, " . . . such transfers surely can be characterized as fraudulent, so long as the debtor had the requisite fraudulent

intent." *Tavenner*, *supra*, at 407. The court, at trial, had gleaned a number of facts surrounding the transfer which permitted the Fourth Circuit to affirm the judgment in favor of the Trustee. It is interesting to note that the property transferred, the proceeds of a personal injury settlement, if retained by the Debtor in his bank account, would have been exempt under Virginia law, *Tavenner*, *supra*, at page 406.

These two recent Court of Appeals decisions demonstrate that while mere exemption planning does not give rise to a claim of fraudulent transfer, additional surrounding facts must be examined to determine if the actual transfer has crossed the line. It was that analysis that the Ninth Circuit's Amended Opinion precludes. Other decisions outside of the Ninth Circuit reflect the split in the law. *In re Wadley*, 263 B.R. 857 (Bk. SD Ohio 2001) highlights what the Ninth Circuit has foreclosed in this case. In *Wadley*, the debtors purchased a motorcycle, sold it prepetition, and filed bankruptcy. They sought to exempt, in their bankruptcy, a purchase of whole life insurance obtained through use of the motorcycle sale proceeds. While the trustee in that case failed to object to exemptions, he did file a complaint to recover the proceeds from the sale of the motorcycle. The trustee asserted that the conversion of the proceeds from the sale of the motorcycle into exempt assets was a fraudulent act. The bankruptcy court stressed that "extrinsic evidence" of fraud can take a transfer beyond permissible exemption planning into the area of a fraudulent transfer. That evidence includes such traditional badges of fraud as a transfer immediately prior to bankruptcy, conversion of a large amount of assets, whether or not the transfer was a reaction to a judgment

against the debtor, and other factors. See generally *Wadley*, *supra*, at page 859-860. In *Wadley*, the bankruptcy court ultimately found no fraudulent transfer because of the relatively small amount of value in the motorcycle that was involved in the transfer, $12,000.00. *Wadley*, *supra*, at page 861. The transfer in the case before this Court, by contrast, was $1.4 million, and was made in conjunction with numerous other transfers by Stern in direct response to the Arbitration Award. What is of consequence is that *Wadley* demonstrates that there must be a factual inquiry undertaken to determine the line between exemption planning and fraudulent transfer. See, also, *In re Lapes*, 254 B.R. 501 (Bk. SD Florida 2000), in which the bankruptcy court refused to permit the transfer to stand where non-exempt assets were used to acquire a homestead in circumstances akin to *Sholdan*, *supra*.

Judge Alarcón in dissent set forth an analysis which would have placed the Ninth Circuit in conformity with these other decisions, 345 F.3d at page 1045 and following. By contrast, the majority has created a conflict among the circuits on an important area of bankruptcy law.

This conflict among the circuits and resulting uncertainty in the law as it pertains to the relationship between exemption planning and fraudulent transfer law causes uncertainty to the bar in providing guidance to clients, uncertainty to bankruptcy trustees as to their avoidance powers, and uncertainty to the lower federal courts in dealing with issues presented with regard to fraudulent transfer and asserted related exemption planning.

This Court has a long tradition of granting certiorari in bankruptcy cases that present important issues of administration of the bankruptcy laws and that are of first

impression in this Court, see, e.g., *Reading Company v. Brown*, 391 U.S. 471 (1968) (status of claim based on receiver's negligence under the Act), or where the circuits have differed on difficult questions of bankruptcy law, see e.g., *Segal v. Rochelle*, 382 U.S. 375 (1966) (issue of loss-carryback under the Act). This tradition has carried through to this day. *See Yates v. Henton*, *supra*. Such tradition of review requires that the important issues of first impression and circuit split present here be resolved by this Court.

CONCLUSION

The Petition for Writ of Certiorari should be granted.

Respectfully submitted,

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345 F.3d 1036

United States Court of Appeals,
Ninth Circuit.

In re Steven H. STERN, Debtor,
David A. Gill, Chapter 7 Trustee, Appellant,
v.
Steven H. Stern, Appellee.
In re Steven H. Stern, Debtor,
Steven H. Stern, Appellant,
v.
David A. Gill, Chapter 7 Trustee, Appellee,
and
Dove Audio, Inc., Plaintiff.

Nos. 00-56431, 00-56526.

Argued and Submitted June 5, 2002.
Filed Feb. 4, 2003.
Amended Opinion Filed Oct. 7, 2003.

Affirmed.

Alarcon, Senior Circuit Judge, filed opinion concurring in part and dissenting in part, and voted to grant rehearing.

Richard D. Burstein, Danning, Gill, Diamond & Kollitz, Los Angeles, CA, for the appellant.

David R. Weinstein (argued), Sharon Z. Weiss (briefed), Weinstein, Eisen & Weiss, Los Angeles, CA, for the appellees.

Appeal from the United States District Court for the Central District of California; Gary A. Feess, District Judge, Presiding. D.C. No. CV-98-07415-GAF, CV-98-07415-GAF.

Before ALARCON, SILVERMAN and RAWLINSON, Circuit Judges.

ORDER AND AMENDED OPINION

RAWLINSON, Circuit Judge.

ORDER

The opinion filed on February 4, 2003, is hereby amended. With this amendment, a majority of the panel has voted to deny the petition for rehearing and the alternative petition for rehearing en banc.

Judges Silverman and Rawlinson voted to deny the petition for rehearing and the alternative petition for rehearing en banc. Judge Alarcon voted to grant the petition for rehearing and recommended granting the alternative petition for rehearing en banc.

The full court has been advised of the alternative petition for rehearing en banc, and no active judge of the court has requested a vote on rehearing the matter en banc. Fed. R.App. P. 35.

The petition for rehearing and alternative petition for rehearing en banc filed on February 12, 2003 are DENIED.

No additional petitions for rehearing will be accepted in this case.

OPINION

David A. Gill, Bankruptcy Trustee, ("Trustee") appeals the district court's decision affirming the bankruptcy court's order, which granted summary judgment in favor of the debtor Steven Stern ("Stern"). Stern cross-appeals the district court's determination that Stern's pension plan funds are not excluded from the bankruptcy estate.

Stern filed for bankruptcy after the entry of a sizeable judgment against him in an arbitration proceeding. We must determine whether the transfer of proceeds from an Individual Retirement Account ("IRA") into a Profit Sharing Pension Plan was a fraudulent transfer, subject to avoidance by the Trustee.[1]

Constrained by our precedent, we AFFIRM the district court's holding that, although the pension plan was properly included within the bankruptcy estate, the pension plan assets were exempt from distribution to Stern's creditors.

I.
Background

Stern's retirement planning commenced with the creation of a tax-qualified profit-sharing plan in 1974 ("1974 Plan").[2] In 1978, Stern terminated the 1974 Plan and created a qualified, defined benefit pension plan ("1978 Plan"). In 1989, Stern terminated the 1978 Plan and transferred the plan assets into an IRA account ("IRA").

Stern became embroiled in a business dispute with Dove Audio, Inc. in 1991. The dispute culminated in an arbitration award of over $4.5 million dollars against Stern. At about the same time, Stern hired Margaret

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[1] The remaining creditors did not actively participate in the appeal.

[2] The retirement plans were established under the auspices of Steven H. Stern, Inc., and benefitted Stern and his then-wife Sharma, who were both employees of Stern, Inc.

Mayersohn ("Mayersohn"), with whom he became romantically involved, and later married.

In April 1992, Stern created a Profit Sharing Plan ("1992 Pension Plan") with Mayersohn and Stern as beneficiaries. On October 22, 1992, the Los Angeles Superior Court issued a writ of attachment to secure the arbitration award. The next day, Stern executed the Plan Documents for the 1992 Pension Plan and, a few days later, transferred the proceeds of his IRA into the 1992 Pension Plan. Dove filed a fraudulent transfer action in state court, contending that Stern's transfer of funds from his IRA into the 1992 Pension Plan was fraudulently designed to shield his assets from creditors. Stern, in turn, initiated a voluntary Chapter 7 bankruptcy proceeding. The creditors removed the fraudulent transfer action to the bankruptcy court as an adversary proceeding.

Stern filed a Motion for Summary Judgment in the core bankruptcy proceeding, seeking to exclude the assets of the 1992 Pension Plan from the bankruptcy estate. Stern also sought summary judgment on the fraudulent transfer claim in the adversary proceeding.

The bankruptcy court ruled that the 1992 Pension Plan was excluded from the bankruptcy estate because it was a qualified plan under the provisions of the Employee Retirement Income Security Act of 1974 ("ERISA"). The bankruptcy court also concluded that, although the 1992 Pension Plan assets were not excluded from the estate under California law, the 1992 Pension Plan's assets were exempted from creditors' claims under California law. Finally, the bankruptcy court held that Stern's transfer of assets from the IRA to the exempt 1992 Pension Plan was

not fraudulent. The creditors appealed the bankruptcy court's rulings to the district court.

The district court rendered the following rulings on appeal:

1. The 1992 Pension Plan was not ERISA qualified;

2. The 1992 Pension Plan was not excludable under state law;

3. The 1992 Pension Plan was exempt under California law; and

4. The transfer of assets from Stern's IRA to the 1992 Pension Plan was not fraudulent.

Stern appeals the district court's ruling that the 1992 Pension Plan was not ERISA-qualified. The Trustee appeals the district court's rulings that the 1992 Pension Plan was exempt under California law, and that the transfer of assets from the IRA to the 1992 Pension Plan was not fraudulent.

II.
Standard of Review

We review the bankruptcy court's grant of summary judgment *de novo. Clicks Billiards, Inc. v. Sixshooters, Inc.,* 251 F.3d 1252, 1257 (9th Cir.2001). We must determine whether, viewing the evidence in the light most favorable to the nonmoving party, genuine issues of fact remain for trial. *Oliver v. Keller,* 289 F.3d 623, 626 (9th Cir.2002). We also must determine whether the bankruptcy court correctly applied the relevant substantive law. *Id.*

"We review the district court's decision on appeal from the bankruptcy court *de novo,* without giving deference to the district court's conclusions." *Harmon v. Kobrin (In re Harmon),* 250 F.3d 1240, 1245 (9th Cir.2001) (citation omitted). Because the facts in this case are virtually undisputed, we focus on the court's application of the law to the facts.[3]

III.
Discussion

A. *ERISA – Qualified Status of the 1992 Pension Plan*

If the 1992 Pension Plan was ERISA-qualified, the assets in the plan were excluded from the bankruptcy estate. *See Patterson v. Shumate,* 504 U.S. 753, 757-58, 112 S.Ct. 2242, 119 L.Ed.2d 519 (1992); *Barkley v. Conner (In re Conner),* 73 F.3d 258, 259-60 (9th Cir.1996). The status of the pension plan is determined as of the date of the bankruptcy filing. *Lowenschuss v. Selnick (In re Lowenschuss),* 171 F.3d 673, 680 (9th Cir.1999).

It is undisputed that, as of the date of his bankruptcy filing, Stern was married to Mayersohn, the only other beneficiary of the 1992 Pension Plan. Prior to the

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[3] The Trustee objected to consideration of certain affidavits submitted by Stern in support of his summary motion. However, the affidavits were in compliance with the requirements of Rule 56(e) of the Federal Rules of Civil Procedure. *Block v. City of Los Angeles,* 253 F.3d 410, 419 (9th Cir.2001) (stating that affidavits must be based upon personal knowledge and contain admissible evidence). Contrary to the Trustee's assertion, the affidavits were not so inconsistent with deposition testimony that the bankruptcy court abused its discretion in considering the affidavits.

marriage, Mayersohn was the sole employee of the 1992 Pension Plan.[4] Absent at least one employee beneficiary, a pension plan is not ERISA-qualified. *See Peterson v. Am. Life & Health Ins. Co.,* 48 F.3d 404, 407-08 (9th Cir.1995).

Although Stern acknowledged the applicability generally of *In re Lowenschuss,* he challenges its applicability specifically to the facts of this case. Relying upon *Peterson,* Stern contended that his marriage to Mayersohn did not alter the ERISA-qualified status of the 1992 Pension Plan.

We agree with the district court that the fact that *Peterson* concerned an employee welfare benefit plan and *In re Lowenschuss* addressed a pension plan is outcome determinative.

29 U.S.C. § 1002(1) defines an ERISA-qualified welfare benefit plan as one "established or maintained . . . for the purpose of providing [benefits] for its participants or their beneficiaries[.]" 29 U.S.C. § 1002(1) (West 1999). In contrast, a pension plan is ERISA-qualified only "to the extent that by its express terms or as a result of surrounding circumstances [the pension plan] provides retirement income to employees . . . " 29 U.S.C. § 1002(2)(A)(i) (West 1999).

Taking into account the welfare benefit plan definition's focus on the past and the pension plan definition's emphasis on the present, *Peterson* and *In re Lowenschuss*

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[4] Stern, as sole owner of the 1992 Pension Plan's sponsor, did not fit within the definition of employee. *See Peterson v. Am. Life & Health Ins.,* 48 F.3d 404, 408 (9th Cir.1995).

are easily reconciled. Under the rationale of *Peterson,* ERISA qualification for a welfare benefit plan is determined after considering the purpose of the plan when it was established or as it is maintained. 48 F.3d at 407-08. In *In re Lowenschuss,* however, we are instructed to assess ERISA qualification for a pension plan by gauging whether there is at least one extant employee beneficiary. 171 F.3d at 680. Under *In re Lowenschuss,* the assessment is made as of the bankruptcy filing date. *Id.*

There is no dispute that as of the bankruptcy filing date, the 1992 Pension Plan covered an owner and the spouse of an owner, neither of which met the definition of employee. *See Peterson,* 48 F.3d at 408; *see also* 29 C.F.R. § 2510.3 3(c)(1). The district court properly applied *In re Lowenschuss* and determined that the 1992 Pension Plan was not ERISA-qualified at the time of the bankruptcy filing. As a result, the assets of the 1992 Pension Plan were not exempt from the bankruptcy estate by virtue of ERISA qualification.

B. *Exemption of the 1992 Pension Plan Under California Law*[5]

Cal.Civ.Proc.Code § 704.115(b) provides: "All amounts held, controlled, or in process of distribution by a private retirement plan, for the payment of benefits as an annuity, pension, retirement allowance, disability payment, or death benefit from a private retirement plan are exempt."

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[5] 11 U.S.C. § 522(b) permits the debtor to claim exemptions under state law.

The Trustee does not take issue *per se* with the applicability of Cal.Civ.Proc.Code § 704.115(b). Rather, the Trustee challenges the exemption on the basis that Stern's transfer of assets from the IRA into the 1992 Pension Plan was fraudulent. That brings us to the final issue before us.

C. *Transfer of Assets Into the 1992 Pension Plan*

The Trustee vigorously advocates that Stern's transfer of assets from his IRA into the 1992 Pension Plan was fraudulent, and therefore, the assets are not exempt from the reach of creditors.

The Trustee's Fourth Amended Complaint asserted claims for fraudulent transfer pursuant to Cal. Civ.Code §§ 3439.04(a); 3439.04(b)1-2 and 3439.05.[6]

Cal. Civ.Code § 3439.04(a) and (b) provide:

> § 3439.04. Transfers fraudulent as to present and future creditors.
>
> A transfer made or obligation incurred by a debtor is fraudulent as to a creditor, whether the creditor's claim arose before or after the transfer was made or the obligation was incurred, if the debtor made the transfer or incurred the obligation as follows:
>
> (a) With actual intent to hinder, delay, or defraud any creditor of the debtor.

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[6] These code provisions encompass actual and constructive fraud. *See Plotkin v. Pomona Valley Imports, Inc. (In re Cohen),* 199 B.R. 709, 716, nn. 7, 8 (B.A.P. 9th Cir.1996).

> (b) Without receiving a reasonably equivalent value in exchange for the transfer or obligation, and the debtor:
>
> (1) Was engaged or was about to engage in a business or a transaction for which the remaining assets of the debtor were unreasonably small in relation to the business or transaction; or
>
> (2) Intended to incur, or believed or reasonably should have believed that he or she would incur, debts beyond his or her ability to pay as they became due.

Cal. Civ.Code § 3439.04.

> § 3439.05. Transfers fraudulent as to present creditors.
>
> A transfer made or obligation incurred by a debtor is fraudulent as to a creditor whose claim arose before the transfer was made or the obligation was incurred if the debtor made the transfer or incurred the obligation without receiving a reasonably equivalent value in exchange for the transfer or obligation and the debtor was insolvent at that time or the debtor became insolvent as a result of the transfer or obligation.

Cal. Civ.Code § 3439.05.

On appeal, only the Fourth, Fifth and Sixth Claims for Relief, related solely to the IRA transfer, are at issue. In the Fourth Claim for Relief, the Trustee alleged that Stern and his Pension Plan effectuated the IRA transfer "with the specific intent to hinder, delay and to defraud creditors of the Debtor."

In the Fifth Claim for Relief, the Trustee alleged that Stern "did not receive reasonably equivalent value in exchange for the IRA transfer."

In the Sixth Claim for Relief, the Trustee alleged that Stern "was insolvent at the time of the IRA Transfer, or . . . became insolvent as a result of the IRA transfer."[7]

We review the district court's determination through the applicable evidentiary lens. *See Anderson v. Liberty Lobby,* 477 U.S. 242, 254, 106 S.Ct. 2505, 91 L.Ed.2d 202 (1986) ("[I]n ruling on a motion for summary judgment, the judge must view the evidence presented through the prism of the substantive evidentiary burden.").

The appropriate evidentiary standard in this case is a matter of some dispute. We have previously ruled in a bankruptcy action involving state law exemptions that proof of fraud "must ordinarily be made by evidence which is clear and convincing." *Love v. Menick (In re Love),* 341 F.2d 680, 682 (9th Cir.1965) (citation and internal quotation marks omitted).[8] However, the United States Supreme Court more recently ruled, in *Grogan v. Garner,* 498 U.S. 279, 111 S.Ct. 654, 112 L.Ed.2d 755 (1991), that proof of fraud for the purpose of the nondischargeability provision of the Bankruptcy Code is governed by "the ordinary preponderance-of-the-evidence standard." *Id.* at 291.

Admittedly, *Grogan* addressed exceptions to the discharge of debts, as provided in 11 U.S.C. § 523, and this

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[7] The Fourth Claim for Relief states a claim for actual fraud. The Fifth and Sixth Claims for Relief assert constructive fraud claims. *See Mejia v. Reed,* 31 Cal.4th 657, 3 Cal.Rptr.3d 390, 74 P.3d 166 (2003).

[8] We are aware that various bankruptcy courts have adopted a preponderance of the evidence standard burden of proof for proceedings under 11 U.S.C. § 548. *See e.g., Model Imperial v. Hamilton Bank,* 250 B.R. 776 (S.D.Fla.2000). However, those cases are not binding precedent, as is *In re Love.*

case concerns eligibility for state law exemptions under 11 U.S.C. § 522. Nevertheless, we are persuaded that the ruling in *Grogan* implicitly overruled our holding in *In re Love.*

We recently clarified that "circuit precedent, authoritative at the time that it issued, can be effectively overruled by subsequent Supreme Court decisions that 'are closely on point,' even though those decisions do not expressly overrule the prior circuit precedent." *Miller v. Gammie,* 335 F.3d 889, 899 (9th Cir.2003) (en banc) (citation omitted). We are now instructed that we are "bound not only by the holdings of [Supreme Court] decisions but also by their 'mode of analysis.' *Id.* at 900 (citation omitted)." [T]he issues decided by the higher court need not be identical in order to be controlling. Rather, the " . . . court . . . must have undercut the theory or reasoning underlying the prior circuit precedent in such a way that the cases are clearly irreconcilable." *Id.* at 900.

Grogan's "mode of analysis" definitively "undercuts the theory" of *In re Love* that proof of fraud sufficient to negate a state law exemption must be clear and convincing. In *Grogan,* the Supreme Court reasoned that "in the context of provisions designed to exempt certain terms from discharge, a debtor has [no] interest in discharge sufficient to require a heightened standard of proof." 498 U.S. at 286, 111 S.Ct. 654. Rather, "[r]equiring the creditor to establish by a preponderance of the evidence that [the assets are non-exempt] reflects a fair balance between the[ ] conflicting interests" of giving debtors a fresh start and protecting creditors who are victims of fraud on the part of the debtor. *Id.* at 287, 111 S.Ct. 654.

The reasoning of *Grogan* warrants a conclusion that our prior precedent, *In re Love,* has been implicitly overruled. No principled basis exists to distinguish between actual fraud and constructive fraud on the one hand, or between nondischargeability of debts and exemption of assets on the other.

Accordingly, we view the evidence in this case in light of the preponderance of the evidence standard of proof. Even so, summary judgment was appropriately entered on behalf of the debtor.

We are constrained by our prior opinion in *Wudrick v. Clements,* 451 F.2d 988 (9th Cir.1971). In that case, we ruled "that the purposeful conversion of nonexempt assets to exempt assets on the eve of bankruptcy is not fraudulent per se." *Id.* at 989 (citation omitted).

The facts of *Wudrick* are not unlike our case.

> When bankruptcy appeared inevitable, Mr. and Mrs. Roon consulted experienced bankruptcy counsel. One of the things they did on his advice to enhance their exemptions was to refinance their 1966 Chevrolet. The bank loaned them $2,325 on the car. From this amount they paid off the previous car loan and their attorney's fees, and deposited $800 in the Union Federal Savings & Loan Association. They then filed petitions in bankruptcy. They claimed that the $800 account was exempt from execution under California [law] and was therefore exempt under section 6 of the Bankruptcy Act, 11 U.S.C. § 24, though the automobile would not have been.

Id.

In reversing the district court's determination that Wudrick engaged in a fraudulent transfer, we clarified

that "[t]he finding of fraud was based solely on the fact that nonexempt assets were deliberately converted to exempt assets just prior to filing the bankruptcy petition." *Id.* at 990. We explained that this "evidence was insufficient as a matter of law to establish fraud." *Id.* Our analysis was impliedly affected by the clarification that a different conclusion might be reached "if on the eve of bankruptcy a debt were created with no intention of repaying the creditor. . . . " *Id.*

Here, the principal evidentiary inference relied upon by the Trustee is that non-exempt assets were converted to exempt assets immediately prior to bankruptcy. But, as *Wudrick* demonstrates, this inference is insufficient as a matter of law to establish a fraudulent transfer. *See Jackson v. Grover (In re Jackson),* 472 F.2d 589, 590 (9th Cir.1973).

The dissent cites *In re Love* in an effort to distinguish *Wudrick.* However, *In re Love* actually supports a finding of exemption. In that case we recognized that "the exemption statutes of California are applied with liberality." 341 F.2d at 682 (citations omitted). We also clarified that the exemption determination is to be determined "upon the basis of conditions existing at the time of the filing of the bankruptcy petition." *Id.* (citations omitted). When Stern's bankruptcy petition was filed, the assets in question "rested in [the 1992 Pension Plan] which . . . enjoyed an exempt status." *See id.*

The dissent also cites *Acequia Inc. v. Clinton, (In re Acequia, Inc.*), 34 F.3d 800 (9th Cir.1994) in support of its position. However, that case is inapposite because the property transferred did not enjoy an exempt status when the bankruptcy petition was filed. The rationale of

Wudrick is inapplicable to a situation such as that presented in *Acequia,* but completely pertinent to the case at hand, where assets are converted to an exempt status pre-bankruptcy.

At bottom, the "badges of fraud" articulated in the dissent merely rephrase the argument that Stern transferred funds from his IRA account into the 1992 Pension Plan Account on the eve of bankruptcy. In such a circumstance, we are persuaded that *Wudrick* controls.

Aside from the conversion of non-exempt assets into exempt assets, which is nonfraudulent "as a matter of law," *see Wudrick,* 451 F.2d at 990, the Trustee and the dissent cite as "badges of fraud" the facts that Stern:

> 1) was sued and lost the arbitration before transferring the funds to the Plan;
>
> 2) testified inconsistently as to his motive for transferring the funds to the Plan;
>
> 3) *may have,* as a result of the 4.5 million dollar arbitration award levied against him, *been insolvent* when he made the transfer;
>
> 4) transferred the funds to the Plan to benefit him and his wife;
>
> 5) transferred all or substantially all of his property into the Plan; and
>
> 6) retained control of the funds following the transfer.

(Dissenting Opinion at pages 1048) (emphasis added).

With the exception of the arbitration loss and the speculative insolvency, the other articulated badges of fraud are simply restatements of the accusation that Stern

converted nonexempt assets into exempt assets, an accusation that cannot support a finding of fraud. *See Wudrick,* 451 F.2d at 990. A similar fate awaits the claim that Stern "may have been insolvent." We have consistently discounted speculative assertions when raised in defense of a summary judgment motion. *See, e.g., Paladin Assoc., Inc. v. Montana Power Co.,* 328 F.3d 1145, 1161 (9th Cir.2003). We are left with the fact that Stern lost a multimillion dollar arbitration. That single unspectacular fact does not meet a preponderance of the evidence burden of proof.

Accordingly, we AFFIRM the district court's rulings that the 1992 Pension Plan was not ERISA-qualified; that the 1992 Pension Plan was exempt under California law; and that the transfer of assets from Stern's IRA to the 1992 Pension Plan was not fraudulent.

AFFIRMED.

ALARCON, Senior Circuit Judge, Concurring in Part, Dissenting in Part.

I concur in the majority's holding that the funds in the Plan were not excludable from Stern's bankruptcy estate. I dissent from the majority's conclusion that the funds in the Plan were exempt from distribution to Stern's creditors under California law. I would hold that the Trustee presented sufficient facts to support an inference that Stern transferred funds into the Plan with the intent to hinder, delay, or defraud his creditors. A fraudulent transfer is not exempt from distribution to creditors under California law. Cal. Civ.Code §§ 3439.04 & 3439.05 (West 2002); *Maddox v. Robertson (In re Prejean),* 994 F.2d 706, 708 (9th Cir.1993). Accordingly, whether the Debtor acted with fraudulent intent is a question that should be

determined after a trial on the merits and a determination of the credibility of the witnesses regarding Stern's intent.

The Trustee presented evidence that on September 15, 1992, Dove Audio, Inc. ("Dove") received an arbitration award of 4,585,000 dollars against Stern. Stern learned of the award on or about September 30, 1992. On October 22, 1992, the Los Angeles Superior Court issued a writ of mandate to secure the payment to Dove of the amount awarded by the arbitrator.

On October 14, 1992, Stern filed for a divorce. The next day, Stern received a Default Judgment of Dissolution of his marriage that included a stipulated property settlement agreement. Between October 19, 1992 and October 21, 1992, pursuant to the property settlement agreement, Stern transferred all his community property, consisting of over 2 million dollars in non-exempt assets, to Sharma Stern. Stern made these transfers without the benefit of property appraisals. Stern retained only supposedly exempt assets and assumed the 4.5 million dollar arbitration award, a community debt, owed to Dove. On October 23, 1992, Stern executed the documents that created the Plan. Later in the same month, Stern rolled 1.4 million dollars from his IRA into the Plan. On November 2, 1992, Stern filed for bankruptcy. Stern dismissed the Chapter 11 action on December 22, 1992, after the bankruptcy judge indicated that she would appoint a trustee for Stern's estate.

In July 1993, Dove filed an action in the Los Angeles Superior Court in which it alleged that Stern had fraudulently transferred the 1.4 million dollars into the Plan to shield his estate from his creditors. On August 11, 1995 while the fraudulent conveyance action was pending in

state court, Stern filed a Chapter 7 bankruptcy petition (the "core proceeding"). In the fall of 1995, Dove transferred the fraudulent conveyance action (the "adversary proceeding") to the bankruptcy court. On June 26, 1996, the Trustee was authorized to intervene in the adversary proceeding.

On or about March 27, 1998, Stern filed a motion for summary judgment in the core proceeding. He sought to prevent the money in the Plan from being included in the bankruptcy estate. He argued that: (1) the Plan is excludable from the bankruptcy estate as ERISA-qualified; (2) the Plan is exempt from creditor distribution under California law; and (3) even if there had been a fraudulent transfer, the Plan would still be exempt. The Trustee responded on April 27, 1998. The bankruptcy court agreed with Stern's arguments. It held that the Plan was excluded from the estate as ERISA-qualified and that it was also exempt under California law.

On or about May 11, 1998, Stern moved for summary judgment on the fraudulent transfer claims in the adversary proceeding. Stern asserted that there was no transfer. He asserted in the alternative that even if there had been a transfer, the Trustee could not show that it was fraudulent. In response, the Trustee disputed Stern's legal arguments and asserted that there was a question of fact regarding Stern's credibility and his intent regarding the transfer. The bankruptcy court concluded that there was nothing improper about transferring assets into an exempt retirement fund on the eve of bankruptcy.

The Trustee timely appealed the bankruptcy court's rulings on summary judgment to the district court. On August 9, 2000, the district court concluded that the funds

in the Plan were not excludable as ERISA-qualified. It also concluded that the funds were exempt from distribution to creditors under California law because the Trustee failed to present evidence of fraud beyond the mere transfer of funds on the eve of bankruptcy.

Under California law, funds held in a "private retirement plan" are exempt from distribution to creditors. *Cheng v. Gill (In re Cheng),* 943 F.2d 1114, 1116 (9th Cir.1991); Cal.Civ.Proc.Code § 704.115(b)-(e) (West 2002). Corporate plans are entitled to complete exemption even where the corporation sponsoring the plan is closely held and its sole shareholder, director, and chief executive officer is the debtor. *In re Cheng,* 943 F.2d at 1115-17. The Plan in the instant case is a corporate plan, sponsored by Stern, Inc., and is therefore exempt. Stern argues that even if we assume that he transferred the funds into the Plan to defraud his creditors, the funds nevertheless remain exempt as part of the corporate plan. I disagree. I would hold that it was error for the district court to uphold summary judgment in favor of Stern where the Trustee presented evidence of fraud, beyond the mere transfer of property on the eve of bankruptcy.

A transfer may be avoided under California law if it was made with the "actual intent to hinder, delay, or defraud any creditor of the debtor," or if it was made "[w]ithout receiving a reasonably equivalent value in exchange for the transfer . . . . " Cal. Civ.Code §§ 3439.04 & 3439.05 (West 2002); *Maddox v. Robertson (In re Prejean),* 994 F.2d 706, 708-09 (9th Cir.1993). A transfer may also be avoided where there is actual fraud. *Love v. Menick,* 341 F.2d 680, 682-83 (9th Cir.1965); *In re Moffat,* 107 B.R. 255, 266 (Bankr.C.D.Cal.1989). Fraudulent intent may be

shown through circumstantial evidence of actual intent to defraud, or "badges of fraud." Badges of fraud include:

> (1) actual or threatened litigation against the debtor;
>
> (2) a purported transfer of all or substantially all of the debtor's property; (3) insolvency or other unmanageable indebtedness on the part of the debtor; (4) a special relationship between the debtor and the transferee; and, after the transfer, (5) retention by the debtor of the property involved in the putative transfer.
>
> The presence of a single badge of fraud may spur mere suspicion; the confluence of several can constitute conclusive evidence of actual intent to defraud, absent "significantly clear" evidence of a legitimate supervening purpose.

Acequia Inc. v. Clinton (In re Acequia Inc.), 34 F.3d 800, 806 (9th Cir.1994) (emphasis and citations omitted); *see also* Cal. Civ.Code § 3439.04 (referring in comment (5) to the consideration courts give to the "badges of fraud").

Citing to on this court's opinion in *Wudrick v. Clements,* 451 F.2d 988 (9th Cir.1971), the majority writes; "Here, the principal evidentiary inference relied upon by Trustee is that non-exempt assets were converted to exempt assets immediately prior to bankruptcy. But, as *Wudrick* demonstrates, this inference is insufficient as a matter of law to establish a fraudulent transfer." Majority opinion at p. 1044.

I respectfully disagree with my esteemed colleagues that *Wudrick* is determinative. It can readily be distinguished from the instant case. In *Wudrick,* Mr. and Mrs. Roon, after consulting experienced bankruptcy lawyers,

refinanced their 1966 Chevrolet automobile. *Id.* at 989. The bank loaned them 2,325 dollars on the car. The Roons used these funds to pay off their previous car loan and their attorney's fees. *Id.* They also deposited 800 dollars in a savings and loan association. *Id.* They then filed bankruptcy petitions. They claimed that the 800 dollar account was exempt from distribution under California law and the Bankruptcy Act. *Id.*

In a companion case, the record showed that Wudrick, on the advice of bankruptcy counsel, obtained a 2,197 dollar loan from a finance company on two vehicles about three weeks before filing his bankruptcy petition. *Id.* He put 1,300 dollars in a credit union. Such funds are exempt from distribution under California law. *Id.*

The Trustee argued in *Wudrick* that "conversion of non-exempt assets to exempt assets on the eve of bankruptcy by creation of a secured debt and deposit of the proceeds in an exempt account is fraudulent as a matter of law and therefore a claim of exemption based on such a transfer is invalid." *Id.* at 990. In rejecting this argument, we held that "[i]t has long been the rule in this and other jurisdictions that the purposeful conversion of nonexempt assets to exempt assets on the eve of bankruptcy is not fraudulent per se." *Id.* at 989 (citing *In re Dudley,* 72 F.Supp. 943, 945-947 (D.Cal.1947), *aff'd per curiam, Goggin v. Dudley,* 166 F.2d 1023 (9th Cir.1948); *Love v. Menick,* 341 F.2d 680, 682-683 (9th Cir.1965)).

The actual holding in *Wudrick* reads as follows:

> Since no more is shown in either case than the intentional conversion of nonexempt property to exempt property, *Love v. Menick, supra,* controls.

> A different case would be presented if on the eve of bankruptcy a debt were created with no intention of repaying the creditor, either by purchasing goods on credit or borrowing money without security. *See Love v. Menick, supra,* at 682-683 F.2d.

Wudrick, 451 F.2d at 990.

There is no showing in this matter that Stern consulted an experienced bankruptcy attorney before he transferred the funds from his IRA into the exempt Plan. He therefore cannot prevail on the argument that he acted in good faith reliance on the advice of his attorney when he transferred the funds and therefore lacked the intent required to deny him a discharge of his debts. *See In re Adeeb,* 787 F.2d 1339, 1343 (9th Cir.1986) (discussing the effect of a debtor's good faith reliance on an attorney's advice). Furthermore, the Trustee presented evidence that he did more than purposefully convert his assets on the eve of bankruptcy.

The Trustee presented evidence that Stern: (1) was sued and lost the arbitration before transferring the funds to the Plan; (2) testified inconsistently as to his motive for transferring the funds to the Plan; (3) may have, as a result of the 4.5 million dollar arbitration award levied against him, been insolvent when he made the transfer; (4) transferred the funds to the Plan to benefit him and his wife; (5) transferred all or substantially all of his property into the plan; and (6) retained control of the funds following the transfer. This evidence demonstrates the presence of several badges of fraud, including actual litigation against Stern, transfer of substantially all of Stern's property, insolvency, and retention of control over the funds after the transfer. This evidence supports an inference of fraudulent intent.

In *Wudrick,* we cited *Love v. Menick* for the rule regarding the purposeful conversion of nonexempt assets to exempt assets. *Wudrick,* 451 F.2d at 989-90. In *Love,* we noted that in *In re Martin,* 217 F.Supp. 937 (D.Or. 1983), the district court cited the prevailing rule "that the purchase of exempt property by an insolvent debtor on the eve of bankruptcy will not, in itself, permit the trustee to disallow the claimed exemption." *Love,* 341 F.2d at 683 (internal quotations omitted). The district court held in *In re Martin,* however, that substantial evidence in the record supported the referee's finding of fraudulent intent and action. *Love,* 341 F.2d at 683. In reconciling the *Martin* decision with the "prevailing rule," we commented in *Love:*

> To harmonize the court's decision with its recognition of the force of . . . the "prevailing rule," we must assume that the record in *Martin* contained some quality of "substantive evidence" of fraudulent intent which we cannot find in the record of the case at hand.

Love, 341 F.2d at 683; *see also In re Dudley,* 72 F.Supp. 943, 945-47 (S.D.Cal.1947) (discussing the "prevailing rule").

Thus, the law of this circuit as reflected in *Wudrick,* and *Love* is as follows: "the purposeful conversion of nonexempt assets to exempt assets on the eve of bankruptcy is not fraudulent per se." *Wudrick,* 451 F.2d at 989. The term "per se" is defined as: "[o]f, in, or by itself; standing alone, without reference to additional facts." Black's Law Dictionary 1162 (7th ed.1999). Therefore, where substantial evidence in the record supports a finding of the debtor's fraudulent intent, property transferred on the eve of bankruptcy is not exempt from distribution to creditors. *See Tavenner v. Smoot,* 257 F.3d 401,

406-09 (4th Cir.2001) (holding that "transfers of exemptible property *are* amenable to avoidance and recovery actions by bankruptcy trustees," and that "such transfers surely can be characterized as fraudulent, so long as the debtor had the requisite fraudulent intent"); *Ford v. Poston,* 53 B.R. 444, 448, 449-50 (D.Va.1984) (stating the general rule that "in the eleventh hour a debtor may convert a part of his property which is not exempt into exempt items for the purpose of placing the property out of reach of his creditors when he claims the exemption," and stating that "[t]he courts have long recognized a limitation of this rule: If the evidence reveals fraud apart and distinct from the mere transfer of non-exempt property into exempt, the debtor has transferred the property with the intent to defraud, hinder, or delay his creditors."); *In re Krantz,* 97 B.R. 514, 522 (Bankr.N.D.Iowa 1989) (discussing the rule that "the act of converting non-exempt property to exempt property is not enough to deny the exemption," but "[t]he actual intent to hinder, delay or defraud one's creditors *is* sufficient to deny an exemption," and that "[b]ecause intent to hinder, delay or defraud is so difficult to prove directly, the Iowa Supreme Court relies on 'badges or indices of fraud' to determine the debtor's intent."). This court's use of the term "per se," in setting forth the rule in *Wudrick* that "the purposeful conversion of non-exempt assets to exempt assets on the eve of bankruptcy is not fraudulent per se," is significant. We did not hold in *Wudrick* that a transfer on the eve of bankruptcy is inexorably exempt from distribution to creditors. The

Majority has simply ignored the significance of the term "per se" in this court's holding in *Wudrick*.[1]

Because the Trustee presented genuine issues of material fact regarding whether Stern acted with fraudulent intent when he transferred funds from his IRA into exempt funds under the Plan, I would reverse the judgment of the district court and remand for a trial on the merits and express findings on the question whether Stern intended to hinder, delay, or defraud his creditors.

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[1] During oral argument, Stern's attorney quoted the holding in *Wudrick*, and attempted to convince this Court that the words "per se" were superfluous. He argued as follows:

> "[T]he purposeful conversion of nonexempt assets to exempt assets on the eve of bankruptcy is not fraudulent per se." And what he [Stern] seems to be saying if I understand him is those two words, "per se," at the end may open up some door, though I've already answered if you assume that opens up a door what could there be behind that door? And the answer is, nothing that changes it. But what's interesting in terms of case analysis, if you take those two words off of there, I can't imagine he could even make the argument, and if *Wudrick* read, "It has long been the rule that the purposeful conversion of nonexempt assets to exempt assets on the eve of bankruptcy is not fraudulent," period . . . I can't even imagine that this would be considered anything but a pure reversal of *Wudrick*, and to suggest that those two words there in that context really mean anything but that, alternatively, is not per se fraudulent. Well, would that open a door? The test has to be what could be behind that door. . . .

317 F.3d 1111

United States Court of Appeals,
Ninth Circuit.

In re Steven H. STERN, Debtor,
David A. Gill, Chapter 7 Trustee, Appellant,
v.
Steven H. Stern, Appellee.
In re Steven H. Stern, Debtor,
Steven H. Stern, Appellant,
v.
David A. Gill, Chapter 7 Trustee, Appellee.
and
Dove Audio, Inc., Plaintiff.

Nos. 00-56431, 00-56526.

Argued and Submitted June 5, 2002.
Filed Feb. 4, 2003.

Affirmed.

Alarcon, Senior Circuit Judge, filed opinion concurring in part and dissenting in part.

Richard D. Burstein, Danning, Gill, Diamond & Kollitz, Los Angeles, CA, for the appellant.

David R. Weinstein (argued), Sharon Z. Weiss (briefed), Weinstein, Eisen & Weiss, Los Angeles, CA, for the appellees.

Appeal from the United States District Court for the Central District of California; Gary A. Feess, District Judge, Presiding. D.C. No. CV-98-07415-GAF, D.C. No. CV-98-07415-GAF.

Before ALARCON, SILVERMAN and RAWLINSON, Circuit Judges.

OPINION

RAWLINSON, Circuit Judge.

David A. Gill, Bankruptcy Trustee ("Trustee"), appeals the district court's decision affirming the bankruptcy court's order, which granted summary judgment in favor of the debtor Steven Stern ("Stern"). Stern cross-appeals the district court's determination that Stern's pension plan funds are not excluded from the bankruptcy estate.

Stern filed for bankruptcy after the entry of a sizeable judgment against him in an arbitration proceeding. We must determine whether the transfer of proceeds from an Individual Retirement Account ("IRA") into a Profit Sharing Pension Plan was a fraudulent conveyance, subject to avoidance by the Trustee.[1]

Constrained by our precedent, we AFFIRM the district court's holding that, although the pension plan was properly included within the bankruptcy estate, the pension plan assets were exempt from distribution to Stern's creditors.

I.
Background

Stern's retirement planning commenced with the creation of a tax-qualified profit-sharing plan in 1974 ("1974 Plan").[2]

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[1] The remaining creditors did not actively participate in the appeal.

[2] The retirement plans were established under the auspices of Steven H. Stern, Inc., and benefitted Stern and his then-wife Sharma, who were both employees of Stern, Inc.

In 1978, Stern terminated the 1974 Plan and created a qualified, defined benefit pension plan ("1978 Plan"). In 1989, Stern terminated the 1978 Plan and transferred the plan assets into an IRA account ("IRA").

Stern became embroiled in a business dispute with Dove Audio, Inc. in 1991. The dispute culminated in an arbitration award of over $4.5 million dollars against Stern. At about the same time, Stern hired Margaret Mayersohn ("Mayersohn"), with whom he became romantically involved, and later married.

In April 1992, Stern created a Profit Sharing Plan ("1992 Pension Plan") with Mayersohn and Stern as beneficiaries. On October 22, 1992, the Los Angeles Superior Court issued a writ of attachment to secure the arbitration award. The next day, Stern executed the Plan Documents for the 1992 Pension Plan and, a few days later, transferred the proceeds of his IRA into the 1992 Pension Plan. Dove filed a fraudulent conveyance action in state court, contending that Stern's transfer of funds from his IRA into the 1992 Pension Plan was a fraudulent transfer designed to shield his assets from creditors. Stern, in turn, initiated a voluntary Chapter 7 bankruptcy proceeding. The creditors removed the fraudulent conveyance action to the bankruptcy court as an adversary proceeding.

Stern filed a Motion for Summary Judgment in the core bankruptcy proceeding, seeking to exclude the assets of the 1992 Pension Plan from the bankruptcy estate. Stern also sought summary judgment on the fraudulent transfer claim in the adversary proceeding.

The bankruptcy court ruled that the 1992 Pension Plan was excluded from the bankruptcy estate because it

was a qualified plan under the provisions of the Employee Retirement Income Security Act of 1974 ("ERISA"). The bankruptcy court also concluded that, although the 1992 Pension Plan assets were not excluded from the estate under California law, the 1992 Pension Plan's assets were exempted from creditors' claims under California law. Finally, the bankruptcy court held that Stern's transfer of assets from the IRA to the exempt 1992 Pension Plan was not a fraudulent transfer. The creditors appealed the bankruptcy court's rulings to the district court.

The district court rendered the following rulings on appeal:

1. The 1992 Pension Plan was not ERISA-qualified;

2. The 1992 Pension Plan was not excludable under state law;

3. The 1992 Pension Plan was exempt under California law; and

4. The transfer of assets from Stern's IRA to the 1992 Pension Plan was not a fraudulent conveyance.

Stern appeals the district court's ruling that the 1992 Pension Plan was not ERISA-qualified. The Trustee appeals the district court's rulings that the 1992 Pension Plan was exempt under California law, and that the transfer of assets from the IRA to the 1992 Pension Plan was not a fraudulent transfer.

II.
Standard of Review

We review the bankruptcy court's grant of summary judgment *de novo*. *Clicks Billiards, Inc. v. Sixshooters,*

Inc., 251 F.3d 1252, 1257 (9th Cir.2001). We must determine whether, viewing the evidence in the light most favorable to the non-moving party, genuine issues of material fact remain for trial. *Oliver v. Keller,* 289 F.3d 623, 626 (9th Cir.2002). We also must determine whether the bankruptcy court correctly applied the relevant substantive law. *Id.*

"We review the district court's decision on appeal from the bankruptcy court *de novo,* without giving deference to the district court's conclusions." *In re Harmon,* 250 F.3d 1240, 1245 (9th Cir.2001) (citation omitted). Because the facts in this case are virtually undisputed, we focus on the court's application of law to the facts.[3]

III.
Discussion

A. *ERISA-Qualified Status of the 1992 Pension Plan*

If the 1992 Pension Plan was ERISA-qualified, the assets in the plan were thereby excluded from the bankruptcy estate. *See Patterson v. Shumate,* 504 U.S. 753, 757-58, 112 S.Ct. 2242, 119 L.Ed.2d 519 (1992); *In re Conner,* 73 F.3d 258, 259-60 (9th Cir.1996). The status of

[3] The Trustee objected to consideration of certain affidavits submitted by Stern in support of his summary judgment motion. However, the affidavits were in compliance with the requirements of Rule 56(e) of the Federal Rules of Civil Procedure. *Block v. City of Los Angeles,* 253 F.3d 410, 419 (9th Cir.2001) (stating that affidavits must be based upon personal knowledge and contain admissible evidence). Contrary to the Trustee's assertion, the affidavits were not so inconsistent with deposition testimony that the bankruptcy court abused its discretion in considering the affidavits.

the pension plan is determined as of the date of the bankruptcy filing. *Lowenschuss v. Selnick (In re Lowenschuss),* 171 F.3d 673, 680 (9th Cir.1999). It is undisputed that, as of the date of his bankruptcy filing, Stern was married to Mayersohn, the only other beneficiary of the 1992 Pension Plan. Prior to the marriage, Mayersohn was the sole employee of the 1992 Pension Plan.[4] Absent at least one employee beneficiary, a pension plan is not ERISA-qualified. *See Peterson,* 48 F.3d at 407-08.

Although Stern acknowledges the applicability generally of *Lowenschuss,* he challenges its applicability specifically to the facts of this case. Relying upon *Peterson,* Stern contends that his marriage to Mayersohn did not alter the ERISA-qualified status of the 1992 Pension Plan.

We agree with the district court that the fact that *Peterson* concerned an employee welfare benefit plan and *Lowenschuss* addressed a pension plan is outcome determinative.

29 U.S.C. § 1002(1) defines an ERISA-qualified welfare benefit plan as one "established or maintained . . . for the purpose of providing [benefits] for its participants or their beneficiaries[.]" 29 U.S.C. § 1002(1) (West 1999). In contrast, a pension plan is ERISA-qualified only "to the extent that by its express terms or as a result of surrounding circumstances [the pension plan] provides retirement income to employees . . . " 29 U.S.C. § 1002(2)(A)(i) (West 1999).

---

[4] Stern, as sole owner of the 1992 Pension Plan's sponsor, did not fit within the definition of employee. *See Peterson v. American Life & Health Ins.,* 48 F.3d 404, 408 (9th Cir.1995).

Taking into account the welfare benefit plan definition's focus on the past and the pension plan definition's emphasis on the present, *Peterson* and *Lowenschuss* are easily reconciled. Under the rationale of *Peterson,* ERISA qualification for a welfare benefit plan is determined after considering the purpose of the plan when it was established or as it is maintained. In *Lowenschuss,* however, we are instructed to assess ERISA qualification for a pension plan by gauging whether there is at least one extant employee beneficiary. Under *Lowenschuss,* the assessment is made as of the bankruptcy filing date.

There is no dispute that as of the bankruptcy filing date, the 1992 Pension Plan covered an owner and the spouse of an owner, neither of which met the definition of employee. *See Peterson,* 48 F.3d at 408; *see also* 29 C.F.R. § 2510.3-3(c)(1). The district court properly applied *Lowenschuss* and determined that the 1992 Pension Plan was not ERISA-qualified at the time of the bankruptcy filing. As a result, the assets of the 1992 Pension Plan were not exempt from the bankruptcy estate by virtue of ERISA qualification.

B. *Exemption of the 1992 Pension Plan Under California Law*[5]

Cal. Civ.Code § 704.115(b) provides: "All amounts held, controlled, or in process of distribution by a private retirement plan, for the payment of benefits as an annuity,

[5] 11 U.S.C. § 522(b) permits the debtor to claim exemptions under state law.

pension, retirement allowance, disability payment, or death benefit from a private retirement plan are exempt."

The Trustee does not take issue *per se* with the applicability of Cal. Civ.Code § 704.115(b). Rather, the Trustee challenges the exemption on the basis that Stern's transfer of assets from the IRA into the 1992 Pension Plan was a fraudulent conveyance. That brings us to the final issue before us.

C. *Transfer of Assets Into the 1992 Pension Plan*

The Trustee vigorously advocates that Stern's transfer of assets from his IRA into the 1992 Pension Plan was fraudulent, and therefore, the assets are not exempt from the reach of creditors.

We are controlled by our prior opinion in *Wudrick v. Clements,* 451 F.2d 988 (9th Cir.1971). In that case, we ruled "that the purposeful conversion of nonexempt assets to exempt assets on the eve of bankruptcy is not fraudulent per se." *Id.* at 989 (citation omitted).

The facts of *Wudrick* are not unlike our case.

> When bankruptcy appeared inevitable, Mr. and Mrs. Roon consulted experienced bankruptcy counsel. One of the things they did on his advice to enhance their exemptions was to refinance their 1966 Chevrolet. The bank loaned them $2,325 on the car. From this amount they paid off the previous car loan and their attorney's fees, and deposited $800 in the Union Federal Savings & Loan Association. They then filed petitions in bankruptcy. They claimed that the $800 account was exempt from execution under California [law] and was therefore exempt under section 6 of the

> Bankruptcy Act, 11 U.S.C. § 24, though the automobile would not have been.

Id.

In reversing the district court's determination that Wudrick engaged in a fraudulent conveyance, we clarified that "[t]he finding of fraud was based solely on the fact that nonexempt assets were deliberately converted to exempt assets just prior to filing the bankruptcy petition." *Id.* at 990. We explained that this "evidence was insufficient as a matter of law to establish fraud." *Id.* Our analysis was impliedly affected by the clarification that a different conclusion might be reached "if on the eve of bankruptcy a debt were created with no intention of repaying the creditor . . . . " *Id.*

Here, the principal evidentiary inference relied upon by the Trustee is that non-exempt assets were converted to exempt assets immediately prior to bankruptcy. But, as *Wudrick* demonstrates, this inference is insufficient as a matter of law to establish a fraudulent conveyance. Moreover, when analyzed under the appropriate evidentiary standard of clear and convincing evidence, *see Anderson v. Liberty Lobby,* 477 U.S. 242, 254, 106 S.Ct. 2505, 91 L.Ed.2d 202 (1986) ("in ruling on a motion for summary judgment, the judge must view the evidence presented through the prism of the substantive evidentiary burden"), the remaining "badges of fraud" relied upon by the Trustee are not supported by sufficient evidence to create a genuine issue of material fact that Stern's transfer of assets was a fraudulent conveyance.

The dissent seeks to distinguish *Wudrick* by citing to *Love v. Menick,* 341 F.2d 680 (9th Cir.1965). However, *Menick* actually supports a finding of exemption. In

Menick, we recognized that "the exemption statutes of California are applied with liberality." *Id.* at 682 (citations omitted). We also noted that a finding of fraud must be established by "clear and convincing" evidence. *Id.* (citation omitted). Finally, we clarified that the exemption determination is to be determined "upon the basis of conditions existing at the time of the filing of the bankruptcy petition." *Id.* (citations omitted). As in *Menick,* when Stern's bankruptcy petition was filed, the assets in question "rested in [the 1992 Pension Plan] which . . . enjoyed an exempt status." *Id.*

The dissent also cites *Acequia Inc. v. Clinton, (In re Acequia, Inc.),* 34 F.3d 800 (9th Cir.1994) in support of its position. However, that case is inapposite because the property transferred did not enjoy an exempt status when the bankruptcy petition was filed. The rationale of *Wudrick* is inapplicable to a situation such as that presented in *Acequia,* but completely pertinent to the case at hand, where assets are converted to an exempt status pre-bankruptcy. At bottom, the "badges of fraud" articulated in the dissent merely rephrase the argument that Stern transferred funds from his IRA account into the 1992 Pension Plan Account on the eve of bankruptcy. In such a circumstance, we are persuaded that *Wudrick* controls.

We recognize that the "badges of fraud" identified by Judge Alarcon in his thoughtful dissent offer some support for the conclusion that there is evidence in the record that could be construed as creating a genuine issue of material fact. However, under *Anderson v. Liberty Lobby, Inc.,* 477 U.S. at 254-56, 106 S.Ct. 2505 and its progeny, this elevated standard of clear and convincing proof must govern our evaluation of the evidence. Although a colorable argument could perhaps be made that there is some

evidence of fraudulent conveyance, we simply believe, after reviewing the record *de novo,* that the existing evidence fails to create a genuine issue of material fact when evaluated under the elevated evidentiary standard governing fraudulent conveyance.

Accordingly, we AFFIRM the district court's rulings that the 1992 Pension Plan was not ERISA-qualified; that the 1992 Pension Plan was exempt under California law; and that the transfer of assets from Stern's IRA to the 1992 Pension Plan was not a fraudulent conveyance.

AFFIRMED.

Opinion by Judge RAWLINSON; Partial Concurrence and Partial Dissent by Judge ALARCON.

ALARCON, Senior Circuit Judge, Concurring in Part, Dissenting in Part:

I concur in the majority's holding that the funds in the Plan were not excludable from Stern's bankruptcy estate. I dissent from the majority's conclusion that the funds in the Plan were exempt from distribution to Stern's creditors under California law. I would hold that the Trustee presented sufficient facts to support an inference that Stern transferred funds into the Plan with the intent to hinder, delay, or defraud his creditors. A fraudulent transfer is not exempt from distribution to creditors under California law. Cal. Civ.Code §§ 3439.04 & 3439.05 (West 2002); *Maddox v. Robertson (In re Prejean),* 994 F.2d 706, 708 (9th Cir.1993). Accordingly, whether the Debtor acted with fraudulent intent is a question that should be determined after a trial on the merits and a determination of the credibility of the witnesses regarding Stern's intent.

The Trustee presented evidence that on September 15, 1992, Dove Audio, Inc. ("Dove") received an arbitration award of 4,585,000 dollars against Stern. Stern learned of the award on or about September 30, 1992. On October 22, 1992, the Los Angeles Superior Court issued a writ of mandate to secure the payment to Dove of the amount awarded by the arbitrator.

On October 14, 1992, Stern filed for a divorce. The next day, Stern received a Default Judgment of Dissolution of his marriage that included a stipulated property settlement agreement. Between October 19, 1992 and October 21, 1992, pursuant to the property settlement agreement, Stern transferred all his community property, consisting of over 2 million dollars in non-exempt assets, to Sharma Stern. Stern made these transfers without the benefit of property appraisals. Stern retained only supposedly exempt assets and assumed the 4.5 million dollar arbitration award, a community debt, owed to Dove. On October 23, 1992, Stern executed the documents that created the Plan. Later in the same month, Stern rolled 1.4 million dollars from his IRA into the Plan. On November 2, 1992, Stern filed for bankruptcy. Stern dismissed the Chapter 11 action on December 22, 1992, after the bankruptcy judge indicated that she would appoint a trustee for Stern's estate.

In July 1993, Dove filed an action in the Los Angeles Superior Court in which it alleged that Stern had fraudulently transferred the 1.4 million dollars into the Plan to shield his estate from his creditors. On August 11, 1995 while the fraudulent conveyance action was pending in state court, Stern filed a Chapter 7 bankruptcy petition (the "core proceeding"). In the fall of 1995, Dove transferred the fraudulent conveyance action (the "adversary

proceeding") to the bankruptcy court. On June 26, 1996, the Trustee was authorized to intervene in the adversary proceeding.

On or about March 27, 1998, Stern filed a motion for summary judgment in the core proceeding. He sought to prevent the money in the Plan from being included in the bankruptcy estate. He argued that: (1) the Plan is excludable from the bankruptcy estate as ERISA-qualified; (2) the Plan is exempt from creditor distribution under California law; and (3) even if there had been a fraudulent transfer, the Plan would still be exempt. The Trustee responded on April 27, 1998. The bankruptcy court agreed with Stern's arguments. It held that the Plan was excluded from the estate as ERISA-qualified and that it was also exempt under California law.

On or about May 11, 1998, Stern moved for summary judgment on the fraudulent transfer claims in the adversary proceeding. Stern asserted that there was no transfer. He asserted in the alternative that even if there had been a transfer, the Trustee could not show that it was fraudulent. In response, the Trustee disputed Stern's legal arguments and asserted that there was a question of fact regarding Stern's credibility and his intent regarding the transfer. The bankruptcy court concluded that there was nothing improper about transferring assets into an exempt retirement fund on the eve of bankruptcy.

The Trustee timely appealed the bankruptcy court's rulings on summary judgment to the district court. On August 9, 2000, the district court concluded that the funds in the Plan were not excludable as ERISA-qualified. It also concluded that the funds were exempt from distribution to creditors under California law because the Trustee failed

to present evidence of fraud beyond the mere transfer of funds on the eve of bankruptcy.

Under California law, funds held in a "private retirement plan" are exempt from distribution to creditors. *Cheng v. Gill (In re Cheng),* 943 F.2d 1114, 1116 (9th Cir.1991); Cal.Civ.Proc.Code § 704.115(b)-(e) (West 2002). Corporate plans are entitled to complete exemption even where the corporation sponsoring the plan is closely held and its sole shareholder, director, and chief executive officer is the debtor. *In re Cheng,* 943 F.2d at 1115-17. The Plan in the instant case is a corporate plan, sponsored by Stern, Inc., and is therefore exempt. Stern argues that even if we assume that he transferred the funds into the Plan to defraud his creditors, the funds nevertheless remain exempt as part of the corporate plan. I disagree. I would hold that it was error for the district court to uphold summary judgment in favor of Stern where the Trustee presented evidence of fraud, beyond the mere transfer of property on the eve of bankruptcy.

A transfer may be avoided under California law if it was made with the "actual intent to hinder, delay, or defraud any creditor of the debtor," or if it was made "[w]ithout receiving a reasonably equivalent value in exchange for the transfer . . . . " Cal. Civ.Code §§ 3439.04 & 3439.05 (West 2002); *Maddox v. Robertson (In re Prejean),* 994 F.2d 706, 708-09 (9th Cir.1993). A transfer may also be avoided where there is actual fraud. *Love v. Menick,* 341 F.2d 680, 682-83 (9th Cir.1965); *In re Moffat,* 107 B.R. 255, 266 (Bankr.C.D.Cal.1989). Fraudulent intent may be shown through circumstantial evidence of actual intent to defraud, or "badges of fraud." Badges of fraud include:

> (1) actual or threatened litigation against the debtor; (2) a purported transfer of all or substantially all of the debtor's property; (3) insolvency or other unmanageable indebtedness on the part of the debtor; (4) a special relationship between the debtor and the transferee; and, after the transfer, (5) retention by the debtor of the property involved in the putative transfer.
>
> The presence of a single badge of fraud may spur mere suspicion; the confluence of several can constitute conclusive evidence of actual intent to defraud, absent "significantly clear" evidence of a legitimate supervening purpose.

Acequia Inc. v. Clinton (In re Acequia Inc.), 34 F.3d 800, 806 (9th Cir.1994) (emphasis and citations omitted); *see also* Cal. Civ.Code § 3439.04 (referring in comment (5) to the consideration courts give to the "badges of fraud").

Citing to this court's opinion in *Wudrick v. Clements,* 451 F.2d 988 (9th Cir.1971), the majority writes; "Here, the principal evidentiary inference relied upon by the Trustee is that non-exempt assets were converted to exempt assets immediately prior to bankruptcy. But, as *Wudrick* demonstrates, this inference is insufficient as a matter of law to establish a fraudulent conveyance." Majority opinion at p. 1116.

I respectfully disagree with my esteemed colleagues that *Wudrick* is determinative. It can readily be distinguished from the instant case. In *Wudrick,* Mr. and Mrs. Roon, after consulting experienced bankruptcy lawyers, refinanced their 1966 Chevrolet automobile. *Id.* at 989. The bank loaned them 2,325 dollars on the car. The Roons used these funds to pay off their previous car loan and their attorney's fees. *Id.* They also deposited 800 dollars in

a savings and loan association. *Id.* They then filed bankruptcy petitions. They claimed that the 800 dollar account was exempt from distribution under California law and the Bankruptcy Act. *Id.*

In a companion case, the record showed that Wudrick, on the advice of bankruptcy counsel, obtained a 2,197 dollar loan from a finance company on two vehicles about three weeks before filing his bankruptcy petition. *Id.* He put 1,300 dollars in a credit union. Such funds are exempt from distribution under California law. *Id.*

The Trustee argued in *Wudrick* that "conversion of nonexempt assets to exempt assets on the eve of bankruptcy by creation of a secured debt and deposit of the proceeds in an exempt account is fraudulent as a matter of law and therefore a claim of exemption based on such a transfer is invalid." *Id.* at 990. In rejecting this argument, we held that "[i]t has long been the rule in this and other jurisdictions that the purposeful conversion of nonexempt assets to exempt assets on the eve of bankruptcy is not fraudulent per se." *Id.* at 989 (citing *In re Dudley,* 72 F.Supp. 943, 945-947 (D.Cal.1947), aff'd per curiam, *Goggin v. Dudley,* 166 F.2d 1023 (9th Cir.1948); *Love v. Menick,* 341 F.2d 680, 682-683 (9th Cir.1965)).

The actual holding in *Wudrick* reads as follows:

> Since no more is shown in either case than the intentional conversion of nonexempt property to exempt property, *Love v. Menick, supra,* controls.
>
> A different case would be presented if on the eve of bankruptcy a debt were created with no intention of repaying the creditor, either by purchasing goods on

> credit or borrowing money without security. *See Love v. Menick, supra,* at 682-683 of 341 F.2d.

Wudrick, 451 F.2d at 990.

There is no showing in this matter that Stern consulted an experienced bankruptcy attorney before he transferred the funds from his IRA into the exempt Plan. He therefore cannot prevail on the argument that he acted in good faith reliance on the advice of his attorney when he transferred the funds and therefore lacked the intent required to deny him a discharge of his debts. *See Adeeb v. Adeeb (In re Adeeb),* 787 F.2d 1339, 1343 (9th Cir.1986) (discussing the effect of a debtor's good faith reliance on an attorney's advice). Furthermore, the Trustee presented evidence that he did more than purposefully convert his assets on the eve of bankruptcy.

The Trustee presented evidence that Stern: (1) was sued and lost the arbitration before transferring the funds to the Plan; (2) testified inconsistently as to his motive for transferring the funds to the Plan; (3) may have, as a result of the 4.5 million dollar arbitration award levied against him, been insolvent when he made the transfer; (4) transferred the funds to the Plan to benefit him and his wife; (5) transferred all or substantially all of his property into the plan; and (6) retained control of the funds following the transfer. This evidence demonstrates the presence of several badges of fraud, including actual litigation against Stern, transfer of substantially all of Stern's property, insolvency, and retention of control over the funds after the transfer. This evidence supports an inference of fraudulent intent.

In *Wudrick,* we cited *Love v. Menick* for the rule regarding the purposeful conversion of nonexempt assets

to exempt assets. *Wudrick,* 451 F.2d at 989-90. In *Love,* we noted that in *In re Martin,* 217 F.Supp. 937 (D. Or. 1983), the district court cited the prevailing rule "that the purchase of exempt property by an insolvent debtor on the eve of bankruptcy will not, in itself, permit the trustee to disallow the claimed exemption." *Love,* 341 F.2d at 683 (internal quotations omitted). The district court held in *In re Martin,* however, that substantial evidence in the record supported the referee's finding of fraudulent intent and action. *Love,* 341 F.2d at 683. In reconciling the *Martin* decision with the "prevailing rule," we commented in *Love:*

> To harmonize the court's decision with its recognition of the force of . . . the "prevailing rule," we must assume that the record in *Martin* contained some quality of "substantive evidence" of fraudulent intent which we cannot find in the record of the case at hand. *Love,* 341 F.2d at 683; *see also In re Dudley,* 72 F.Supp. 943, 945-47 (S.D.Cal.1947) (discussing the "prevailing rule").

Thus, the law of this circuit as reflected in *Wudrick,* and *Love* is as follows: "the purposeful conversion of nonexempt assets to exempt assets on the eve of bankruptcy is not fraudulent per se." *Wudrick,* 451 F.2d at 989. The term "per se" is defined as: "[o]f, in, or by itself; standing alone, without reference to additional facts." Black's Law Dictionary 1162 (7th ed.1999). Therefore, where substantial evidence in the record supports a finding of the debtor's fraudulent intent, property transferred on the eve of bankruptcy is not exempt from distribution to creditors. *See Tavenner v. Smoot,* 257 F.3d 401, 406-09 (4th Cir.2001) (holding that "transfers of exemptible property *are* amenable to avoidance and recovery actions by bankruptcy trustees," and that "such transfers surely can be characterized as fraudulent, so long as the

debtor had the requisite fraudulent intent"); *Ford v. Poston,* 53 B.R. 444, 448, 449-50 (D.Va.1984) (stating the general rule that "in the eleventh hour a debtor may convert a part of his property which is not exempt into exempt items for the purpose of placing the property out of reach of his creditors when he claims the exemption," and stating that "[t]he courts have long recognized a limitation of this rule: If the evidence reveals fraud apart and distinct from the mere transfer of non-exempt property into exempt, the debtor has transferred the property with the intent to defraud, hinder, or delay his creditors."); *In re Krantz,* 97 B.R. 514, 522 (Bankr.N.D.Iowa 1989) (discussing the rule that "the act of converting non-exempt property to exempt property is not enough to deny the exemption," but "[t]he actual intent to hinder, delay or defraud one's creditors *is* sufficient to deny an exemption," and that "[b]ecause intent to hinder, delay or defraud is so difficult to prove directly, the Iowa Supreme Court relies on 'badges or indices of fraud' to determine the debtor's intent."). I note that this court's use of the term "per se" in setting forth the rule in *Wudrick* that "the purposeful conversion of nonexempt assets to exempt assets on the eve of bankruptcy is not fraudulent per se," is significant. The words "per se" should not be ignored.[1]

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[1] At oral argument, Stern's attorney quoted *Wudrick,* and attempted to convince this Court that the words "per se" were superfluous:

> "[T]he purposeful conversion of nonexempt assets to exempt assets on the eve of bankruptcy is not fraudulent per se." And what he [Mr. Burstein, Appellant's counsel] seems to be saying if I understand him is those two words, "per se," at the end may open up some door, though I've already answered if you assume that opens

(Continued on following page)

Because the Trustee presented genuine issues of material fact regarding whether Stern acted with fraudulent intent when he transferred funds from his IRA, which were exempt only to the extent necessary to support him in his retirement, into exempt funds under the Plan, I would reverse the judgment of the district court and remand for a trial and findings on the question whether Stern intended to hinder, delay, or defraud his creditors.

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up a door what could there be behind that door? And the answer is, nothing that changes it. But what's interesting in terms of case analysis, if you take those two words off of there, I can't imagine he could even make the argument, and if *Wudrick* read, "It has long been the rule in this and other jurisdictions that the purposeful conversion of nonexempt assets to exempt assets on the eve of bankruptcy is not fraudulent," period . . . I can't even imagine that this would be considered anything but a pure reversal of *Wudrick,* and to suggest that those two words there in that context really mean anything but that, alternatively, is not per se fraudulent. Well, would that open a door? The test has to be what could be behind that door . . .

UNITED STATES COURT OF APPEALS
FOR THE NINTH CIRCUIT

In re STEVEN H. STERN, Debtor.	Case No. 00-56431, 00-56526 Bk. Case No. SV 95-16165-KL [Chapter 7]
DAVID A. GILL, Chapter 7 Trustee, Appellant, v. STEVEN H. STERN, STEVEN H. STERN as Trustee, etc., et al., Appellees.	Bk. Adv. No. 95-01544-KL PETITION FOR PANEL REHEARING, OR, IN THE ALTERNATIVE, FOR REHEARING EN BANC [Federal Rules of Appellate Procedure 40, 35, Circuit Rules 40-1, 35-1]

APPEAL FROM AN ORDER OF
THE UNITED STATES DISTRICT COURT
FOR THE CENTRAL DISTRICT OF CALIFORNIA
THE HONORABLE GARY A. FEESS,
UNITED STATES DISTRICT JUDGE

(Filed Feb. 12, 2003)

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TABLE OF CONTENTS

		Page
I.	INTRODUCTION AND STATEMENT OF COUNSEL	1
II.	SUMMARY OF ARGUMENT	2
III.	THE STANDARD FOR THE TRUSTEE'S BURDEN OF PROOF AT THE TIME OF TRIAL WOULD ONLY BE A PROPONDERANCE OF THE EVIDENCE	3
IV.	CONCLUSION	6

TABLE OF AUTHORITIES

Cases	Page(s)
Annod Corporation vs. Hamilton & Samuels, 100 Cal. App. 4th 1286, 1293 (2002)	4, 5
Dimidowich v. Bell & Howell, 803 F.2d 1473, 1482 (9th Cir. 1987)	5
Grogan v. Garner, 498 US 279, 286 (1991)	3, 4
In re Pajaro Dunes Rental Agency, Inc., 174 B.R. 557, 573-4 (Bk. ND Cal., 1994)	4
In re Serrato, 214 B.R. 219, 229 (Bk. N.D. Cal. 1997)	4

Liodas vs. Sahadi, 19 Cal. 3d 278, 291-2 (1977).....3, 4, 5

Love vs. Menick, 341 Fd.2 680,. 682 (9th Cir., 1965).....2, 3

Pittman vs. Union Planters National Bank & Trust Company, 118 F.2d 211. 213 (6th Cir. 1941)..... 3

Reddy v. Gonzalez, 8 Cal. App. 4th 118 (1992 5

Whitehouse vs. Six Corporation, 40 Cal. App. 4th 527, 533-534 (1995).....4, 5

Wudrick vs. Clements, 451 F.2d 988 (9th Cir. 1971)..... 2

Statutes

11 USC 523(a) of the Bankruptcy Code..... 3

California Evidence Code Section 115..... 3

Circuit Rules 40-1 1

Federal Rules of Appellate Procedure 40, 35 1

Other Authorities

California Uniform Fraudulent Transfer Act.....3, 4

I.

INTRODUCTION AND STATEMENT OF COUNSEL

Appellant, David A. Gill, as Chapter 7 Trustee ("Trustee"), respectfully requests that the Panel rehear its majority decision reflected in its Opinion filed February 4, 2003 as to the ruling on the Trustee's claims of fraudulent transfer or, in the alternative, that rehearing en banc be granted under Federal Rules of Appellate Procedure 40, 35, Circuit Rules 40-1 and 35-1.

In the opinion of the Trustee's undersigned counsel, the majority erred in concluding that the burden of proof

imposed on the Trustee to establish a fraudulent transfer is "clear and convincing evidence". See Opinion, at page 1544.

The applicable burden of proof is actually only a preponderance of the evidence. Since the clear and convincing evidence conclusion underpins the majority's ultimate ruling, the majority has erred, in the judgment of the Trustee's counsel. The burden of proof was neither briefed nor argued by the parties to this Court, nor was it dealt with in the decision of the District Court. See, Excerpts of Record, Tab 18.

Consequently, the Panel should rehear the matter and conclude that the correct standard is a preponderance of the evidence. At that point, the majority should find itself in agreement with the dissent and rule accordingly.[1]

This issue of the Trustee's burden of proof in a fraudulent transfer case and its effect on the review of the judgment below is a question of exceptional importance and affects this Court's analysis of its precedents on the fraudulent transfer issues present herein. The determination of this issue will dramatically affect all bankruptcy trustees in their avoidance power claims in this circuit and throughout the United States. En banc rehearing is thus also proper.

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[1] The majority and Judge Alarcón are already in agreement that the instant pension plan was not excluded from the bankruptcy estate, Opinion at pages 1540-2, 1545. The Trustee does not request rehearing of that determination.

II.

SUMMARY OF ARGUMENT

At page 1544 of its Opinion, this Court concludes that " . . . a finding of fraud must be established by 'clear and convincing' evidence." From that conclusion, the Court then goes on to say that in evaluating the summary judgment burden placed on the Trustee in light of that standard, the Trustee had failed to create a triable issue of fact. See, page 1545.

For this analysis, this Court relied on its opinion in *Love vs. Menick*, 341 Fd.2 680 (9th Cir., 1965). In so doing, it erred. The standard for the Trustee's burden of proof at the time of trial on a claim of fraudulent transfer is a preponderance of the evidence, under both applicable federal law and as a matter of California law.[2] The burden of proof issue was neither argued nor briefed to this Court, nor is it discussed in the District Court Order.

Consequently, this Court's Opinion contained an error of law requiring rehearing, as it affects the entirety of the majority analysis. Viewed under the proper standard, the majority's analysis must become one with the dissent. Alternatively, en banc determination should be granted because this is a question of exceptional importance, and affects the Court's reading of its prior precedent in *Wudrick vs. Clements*, 451 F.2d 988 (9th Cir. 1971) the centerpiece of this appeal.

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[2] The Trustee proceeded under the actual and constructive fraudulent transfer provisions of the California version of the Uniform Fraudulent Transfer Act. See, Excerpts of Record, Tab 18, pages 6 (1310), 19-20 (1323-4).

III.

THE STANDARD FOR THE TRUSTEE'S BURDEN OF PROOF AT THE TIME OF TRIAL WOULD ONLY BE A PROPONDERANCE OF THE EVIDENCE

In *Love vs. Menick*, *supra*, at page 682, this Court concluded in 1965, in evaluating exemption issues under California law, that proof of fraud " . . . must ordinarily be made by evidence which is 'clear and convincing'." This Court relied solely on *Pittman vs. Union Planters National Bank & Trust Company*, 118 F.2d 211 (6th Cir. 1941). *Pittman*, an action under the Bankruptcy Act, dealt with priority claims to funds and stated, without supporting authority, after discussion of substantive federal cases and Tennessee law, that "[i]t is a truism, requiring no supporting citations, that fraud may not be assumed and must be established by clear and convincing evidence." *Pittman*, *supra*, at page 213. Time has turned its face against this unsupported truism and the *Love* Court's reliance on it.

The Trustee's complaint asserting the fraudulent transfer to the pension plan made the subject of this appeal was brought under the California Uniform Fraudulent Transfer Act, as noted above. Whatever uncertainty may have previously existed under California law as to the burden of proof for establishing fraud was decisively resolved by the California Supreme Court in its 1977 opinion in the case of *Liodas vs. Sahadi*, 19 Cal. 3d 278 (1977), when the Court established that the preponderance of the evidence standard applies to claims of fraud in California. In doing so, the Court relied in part on California Evidence Code Section 115 which establishes preponderance of the evidence in civil cases as the generally applicable standard of proof. See, *Liodas*, *supra*, at pages 291-2.

Similarly, in *Grogan v. Garner*, 498 US 279 (1991), the United States Supreme Court unanimously determined that the standard of proof under 11 USC 523(a) of the Bankruptcy Code to avoid a debtor's discharge for "actual fraud" was a preponderance of the evidence, not clear and convincing proof. The Supreme Court adopted this standard because it was the standard generally applicable in civil cases unless particularly important interests or rights are at stake. See, *Grogan, supra*, at page 286. Such reasoning is similar to that of the California Supreme Court in *Liodas*. No greater interests or rights are present in a civil action to avoid and recover for a fraudulent transfer between litigants in an adversary proceeding, essentially a dispute over money. It is for that reason that the Bankruptcy Court in the case of *In re Pajaro Dunes Rental Agency*, Inc., 174 B.R. 557, 573-4 (Bk. ND Cal., 1994), concluded that constructive fraudulent transfer claims have always been decided based on the standard being a preponderance of the evidence and that actual fraudulent transfer claims should also be subject to the same standard. Accord, *In re Serrato*, 214 B.R. 219, 229 (Bk. N.D. Cal. 1997) (actual intent fraudulent transfer claim under California Uniform Fraudulent Transfer Act proven by a preponderance of the evidence).

The most recent decisions by California appellate courts on the issue are those of the California Court of Appeal in *Whitehouse vs. Six Corporation*, 40 Cal. App. 4th 527, 533-534 (1995), where the court held that the standard for the burden of proof of fraudulent transfer claims under California law is a preponderance of the evidence, and *Annod Corporation vs. Hamilton & Samuels*, 100 Cal. App. 4th 1286 (2002), where the court evaluated a summary judgment in a fraudulent transfer claim under

California law (Uniform Fraudulent Transfer Act) in light of the burden of proof at trial, much like the analysis of the majority and dissent here. The court in *Annod* held the standard for the burden of proof was a preponderance of the evidence, relying on both *Liodas*, *supra*, and *Whitehouse*, *supra*, among other authority. See, *Annod*, *supra*, at page 1293.[3]

It is thus apparent that California law on the issue of the standard for burden of proof in a fraudulent transfer matter is preponderance of the evidence and this Court must so conclude. *Dimidowich v. Bell & Howell*, 803 F.2d 1473, 1482 (9th Cir. 1987).[4]

The majority of this Court thus erred in establishing the standard for burden of proof for the Trustee at the time of trial as clear and convincing evidence. Viewed under a preponderance of the evidence standard, the majority of this Court must reconsider its opinion and conclude, as did the dissent, that the Trustee presented sufficient facts to support an "inference" that Stern transferred the funds into the plan with the requisite intent to hinder, delay or defraud. See, Opinion at 1545.

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[3] *Annod* notes that an earlier California Court of Appeal case adopting a clear and convincing evidence standard, *Reddy v. Gonzalez*, 8 Cal. App. 4th 118 (1992), did so in reliance on a case disapproved by the *Liodas* court. See, *Annod*, *supra*, at page 1293.

[4] It is worth noting that the actual intent claim has three alternative elements in the disjunctive, "hinder, delay *or* defraud," California Civil Code Section 3439.04(a). Only one of them speaks of fraud.

IV.

CONCLUSION

For all the reasons set forth herein, it is respectfully requested that rehearing be granted, or rehearing en banc be granted, that this Court correct its error of law with regard to the standard for the burden of proof applicable to the Trustee, and, that, as the dissent had concluded, determine that the order of the District Court as to the transfer claim and judgment of the Bankruptcy Court must be reversed.[5]

Dated: February 11, 2003

DANNING, GILL, DIAMOND & KOLLITZ, LLP

By: /s/ Richard D. Burstein
Richard D. Burstein
Attorneys for Appellant, David A. Gill, as Chapter 7 Trustee

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[5] The Trustee also draws to the attention of this Court to the fact that the dissent's quotation from the argument of Stern's counsel set forth in the footnote at page 1553 of the Opinion could result in confusion for those who are not parties to the appeal where the word "he" in the third line is followed with brackets and the name "Stern." In fact, Mr. Weinstein's (Stern's counsel) reference to "he" at that point was either to the Appellant's counsel, or to the Trustee himself, because Mr. Weinstein was dealing with the Trustee's argument on appeal as to the effect of the words "per se" in *Wudrick*. It is respectfully requested, upon publication, that Judge Alarcón consider making an appropriate clarification in that footnote.

CERTIFICATE OF COMPLIANCE
CIRCUIT RULES 35-4 and 40-1

I certify that pursuant to Circuit Rule 35-4 or 40-1 the attached Appellant's Petition For Panel Rehearing, Or, In The Alternative, For Rehearing En Banc is: proportionately spaced, has a typeface of 14 points and contains 1,361 words.

Dated: February 11, 2003

DANNING, GILL, DIAMOND & KOLLITZ, LLP

By: /s/ Richard D. Burstein
Richard D. Burstein
Attorneys for Appellant, David A. Gill, as Chapter 7 Trustee

PROOF OF SERVICE

I, MARTHA GONZALEZ, declare:

I am employed by the law firm of DANNING, GILL, DIAMOND & KOLLITZ, LLP, in the County of Los Angeles, State of California. I am employed in the office of a member of the bar of this court at whose direction the service was made. I am over the age of 18 years and am not a party to the within action. My business address is 2029 Century Park East, Third Floor, Los Angeles, California 90067-2904.

PETITION FOR PANEL REHEARING, OR, IN THE ALTERNATIVE, FOR REHEARING EN BANC

on the interested parties addressed as follows:

[SEE ATTACHED SERVICE LIST.]

(By Mail) I placed the document for collection and deposit in the mail. I am familiar with this firm's practice for the collection and processing of correspondence for mailing. Under that practice, the document would be placed in a sealed envelope and deposited with the U.S. Postal Service on that same day with postage thereon fully prepaid at 2029 Century Park East, Third Floor, Los Angeles, California 90067-2904, in the ordinary course of business. The documents served were placed in sealed envelopes and placed for collection and mailing following ordinary business practices.

I declare under penalty of perjury under the laws of the State of California and of the United States of America that the foregoing is true and correct.

Executed on February 11, 2003, at Los Angeles, California.

MARTHA GONZALEZ	Martha Gonzalez
(Type or print name)	(Signature)

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UNITED STATES DISTRICT COURT
FOR THE CENTRAL DISTRICT OF CALIFORNIA

In Re STEVEN H. STERN, Debtor.	**Case No. CV 98-7415-GAF [Consolidated with CV 98-8972 GAF, CV 98-7416 GAF and CV 98-8791]**
DOVE AUDIO, INC., MICHAEL VINER, JERRY LEIDER, and DAVID A. GILL, Chapter 7 Trustee, Appellants, v STEVEN H. STERN, Appellee.	**ORDER RE: APPEAL FROM ORDER OF BANKRUPTCY COURT** (Filed Jul. 27, 2000)

I.

INTRODUCTION

This case presents the question of whether a debtor may lawfully shield assets from his creditors by transferring money from an IRA into a qualified pension and profit sharing plan on the eve of bankruptcy The Bankruptcy Court (Honorable Kathleen T Lax, presiding) found that the transfer was proper pre-bankruptcy planning and that the plan assets were excluded from the bankruptcy estate. Although this Court concludes that the assets were not *excluded* from the estate, the Court concludes that the assets were *exempt* from distribution to creditors under

controlling California law, and accordingly AFFIRMS the order of the bankruptcy court in favor of the debtor

II.

FACTUAL BACKGROUND

A. The Parties

Debtor Steven Stern ("Stern") is a movie director who filed for bankruptcy in 1995 Appellant David A. Gill is the trustee of the bankruptcy estate ("Trustee") Appellants Dove Audio ("Dove") and Jerry Leider are creditors of Stern (collectively, "Creditors"). Appellants appeal from a determination by the bankruptcy court that assets held in the Steven H. Stern, Inc Profit Sharing Plan (the "Plan") are part of the bankruptcy estate. (Statement of Undisputed Facts ("SUF") 1; Trustee's Appendix ("TA") at 365)[1]

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[1] Appeals 98-7416 and 98-8791 are from the order finding that the transfer of money from Stern's personal IRA to the Steven H Stern Profit Sharing Plan was not a fraudulent transfer ("Fraudulent Transfer Appeal") Appeals 98-7415 and 98-8972 are from the order finding that the assets in the Steven H Stern Profit Sharing Plan were excluded from the bankruptcy estate and/or exempted from distribution ("Exclusion/Exemption Appeal")

Stern's Statement of Undisputed Facts in Support of Summary Judgment in the Fraudulent Conveyance action is found at the Trustee's Appendix, pp 364-69 Nearly all of the facts are undisputed *See* Trustee's Statement of Genuine Issues at Trustee's Appendix, pp 394-96, Creditor's Statement of Genuine Issues at Trustee's Appendix, pp 486-502 Because the facts are essentially the same with respect to both appeals, all factual references are to this index unless otherwise noted

B. The "Old" Plans

The assets in the Plan came from an IRA account, but the source of the funds in that account were accrued over about 17 years in other pension plans. The following traces the original sources of those funds.

In March 1974, Steven H Stern, Inc ("Stern, Inc ") established a tax-qualified profit sharing plan ("Old Plan A") (SUF 6, TA at 366) Old Plan A received a favorable qualification letter from the IRS (*Id.*) Stern and his then-wife, Sharma Stern ("Sharma"), were both employees of Stern, Inc. and beneficiaries of Old Plan A. (SUF 7; TA at 366.) Between 1974-1978, Stern, Inc made contributions to Old Plan A. (*Id.*)

In 1978, Stern, Inc terminated Old Plan A and created a qualified defined benefit pension plan ("Old Plan B") in order to take advantage of changing tax law (SUF 8; TA at 366.) This transaction was approved by the IRS. (SUF 9; TA at 366.) Stern and Sharma were the beneficiaries of Old Plan B. (SUF 10; TA at 366.) Between 1978-1989, Stern, Inc made contributions to Old Plan B. (*Id.*)

C. The 1989 Rollover IRA

In 1989, Stern, Inc terminated Old Plan B because its actuaries and administrators determined that the benefits under the plan were fully funded under existing law and such action would avoid potential excise taxes. (SUF 11; TA at 366-67.) Stern, Inc. thus terminated and liquidated the trust that held the assets for Old Plan B and Stern rolled over his beneficial interests into an IRA (SUF 12; TA at 367) Stern did this to avoid paying taxes on the withdrawal of his interests and because it would cost less

for him to maintain an IRA than Old Plan B. (*Id.*) The IRS approved the termination and liquidation of the trust. (*Id.*) The assets were held in the IRA for about three years.

D. The Sterns' Divorce

In the meantime, the Sterns had begun divorce counseling in August 1990 (SUF 19; TA at 368) The Sterns agreed to separate, but decided to reside in the same house until their daughter's wedding on May 10, 1991. (*Id.*) From June-November 1991, Stern was living in British Columbia while working on a film (SUF 20; TA at 368) When he returned in November 1991, Stern moved into a separate residence (*Id.*)

In early 1992, Stern, Inc. hired Margaret Mayersohn and sometime thereafter became involved with her (*See* SUF 14, 17; TA at 367-68) Stern contacted a divorce attorney in May 1992 regarding possible marriage dissolution. (SUF 21, TA at 368.) In June 1992, Stern began another film project in Toronto, Canada. (SUF 22, TA at 368.) He and Sharma agreed to commence formal divorce proceedings when he returned to California (*Id.*) Stern returned in October 1992 (SUF 23; TA at 369) On October 14, 1992, Stern filed a petition for Dissolution of Marriage (Creditors' Genuine Issues ("CGI") e, TA at 497)

E. The $4.5 Million Arbitration Award

On the business front, Stern was involved in a project with Dove, which became the subject of a dispute in 1991 (*See* SUF 18, TA at 368.) The dispute led to arbitration and, in September 1992, Dove received an award of $4,585,000 against Stern (*Id.*) Stern learned of this ruling

while in Toronto. (SUF 24, TA at 369.) On October 22, 1992, the Los Angeles Superior Court issued a writ of attachment to secure the arbitration award (CGI h; TA at 498.)

F. The Steven H. Stern, Inc. Profit Sharing Plan

As Stern's marriage was coming to an end and the dispute with Dove was coming to a head, the Steven H Stern, Inc. Profit Sharing Plan ("the Plan") was created Stern is the sole shareholder and owner of the corporate sponsor of the Plan, as well as the Plan's trustee (CGI p, TA at 501.) Mayersohn immediately became a participant in the Plan. (SUF 15; TA at 367) Although the Plan was created as of April 1, 1992 and funded that month, the Plan documents were not executed until October 23, 1992, the day after the writ of attachment of issued in the Dove litigation. (SUF 2; TA at 365; CGI h; TA at 498.) Stern, Inc. made regular contributions to the Plan in 1993 and 1994 to Mayershon's retirement account. (SUF 15, TA at 367.)

G. Stern Rolls his IRA into the Plan

In October 1992, Stern's IRA, which was initially funded with assets from the "Old Plans," was worth approximately $1,525,000 (SUF 25; TA at 369.) In late October 1992, Stern rolled approximately $1 4 million into the Plan. (SUF 25-26; TA at 369, CGI f, TA at 498.)

Stern withdrew money from the Plan in February 1993 when he took a participant loan of $65,000. (SUF 19; TA at 327-28.) Stern paid taxes on the money and has repaid approximately $7,000. (Debtor's Statement of

Uncontroverted Facts in Support of Exclusion/Exemption ("SUF 2") 19; Trustee's Index in Exclusion/Exemption Appeal ("TA2") at 327-28.) In addition, Stern has been taking monthly distributions (approved by the bankruptcy court) since he turned 59 ½ in May 1997. (*Id.*) In August 1995, when Stern filed for bankruptcy, Stern's interest in the Plan was $1,690,000 and Margaret Stern's interest was $7,2000. (SUF2 20; TA2 at 328.)

III.

PROCEDURAL HISTORY

A. The Bankruptcy Action

To recapitulate, in September 1992, Dove obtained an arbitration award against Stern in the amount of $4,585,000. On October 22, 1992, the Los Angeles Superior Court issued a writ of attachment in favor of Dove to secure the arbitration award On October 23, 1992, Stern executed the Plan documents In late October, Stern rolled his IRA proceeds into the Plan A Petition to Confirm Arbitration Award was set for hearing on November 3, 1992 (CGI b; TA at 497.)

On November 2, 1992, Stern filed for Chapter 11 bankruptcy (CGI j; TA at 499) On November 13, 1992, Dove moved for relief from the automatic bankruptcy stay so that it could pursue its action; Dove also moved to dismiss the bankruptcy action or to appoint a trustee. (CGI k; TA at 499) Stern voluntarily dismissed the bankruptcy action on December 22, 1992, after Judge March indicated that she would be appointing a trustee. (CGI l, TA at 500)

In or about July 1993 Dove filed a fraudulent conveyance action in the Los Angeles Superior Court (CGI m; TA at 500; *see* Exh P, TA at 585.) Among the causes of action, Dove alleged that Stern's transfer of funds from his IRA to the Plan was a fraudulent transfer designed to shield his estate from his creditors Specifically, the complaint alleged (1) that by transferring the $1.4 million from his non-exempt IRA to the Plan, Stern intended to hinder, delay and defraud his creditors (Fourth Cause of Action) (Fourth Amended Complaint ¶¶ 23, 41-42; TA at 8, 12); and (2) that Stern did not receive a reasonable equivalent value for the IRA transfer, thus constituting a constructive fraudulent transfer (Fifth and Sixth Causes of Action) (Fourth Amended Complaint ¶¶ 44-53; TA at 13-15). Appellants sought to avoid the transfer or an amount equal to the value of the IRA funds. (*See* TA at 17.)

In August 1995, Stern filed a voluntary Chapter 7 bankruptcy petition. (CGI n; TA at 500.) In the fall of 1995, the creditors removed the fraudulent conveyance action to the bankruptcy court (the "adversary proceeding") [2] (CGI t, TA at 502.) On June 26, 1996, the Trustee was authorized to intervene in the action. (CGI s; TA at 502.)

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[2] Fraudulent conveyance objections must be brought by separate action, not as an objection in the main action 5 *Collier on Bankruptcy* ¶ 548 66(1)

B. Summary Judgment Granted on Exemption/ Exclusion of Pension Plan

On or about March 27, 1998, Stern filed a Motion for Summary Judgment Re Pension Plan Interests in the main bankruptcy proceeding. (TA2 at 1-33.) Stern asserted that the money in the plan should not be included in the bankruptcy estate because (1) the Plan was ERISA qualified, (2) the Plan was excluded as a spendthrift trust under California law; (3) the plan was exempt under California law; and (4) even if there was a fraudulent transfer; the Plan would still be excludable and/or exempt (*Id.*)

The bankruptcy court found that the Plan was excluded from the bankruptcy estate because it was qualified under ERISA (TA2 at 649-50.) The court reasoned that the Plan was funded by money that had been treated as retirement funds for a number of years prior to its deposit in the fund (TA 2 at 652.) The court further found that the fact that Stern married the Plan's only employee did not change the Plan's qualified status [3] (TA2 at 650-53.)

Anticipating that the case would be appealed, the court also addressed the remaining arguments. The court found that the Plan was not excluded from the estate under California law because Stern exercised dominion and control over the Plan (TA2 at 653-54.) However, the

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[3] As discussed below, to qualify under ERISA, a retirement plan must cover "employees." 29 U.S.C. § 1002(2) The spouse of the owner of the business sponsoring the plan is not an "employee" 29 C F R § 2510.3-3(c)(1).

court ruled that the Plan would be exempt under California law, and that the exemption would not be lost even if there was a fraudulent conveyance. (TA2 at 655-60.)

Appellants filed a timely notice of appeal. (TA2 at 580-82.)

C. Summary Judgment on Transfer

In May 1998, Stern moved for summary judgment on the fraudulent transfer claims in the adversary proceeding (Fourth, Fifth and Sixth Causes of Action) Stern asserted that there was no transfer or, if there was, the Trustee[4] could not show a fraudulent transfer as a matter of law. (TA at 22-52.) In addition to disputing Stern's legal arguments, Appellants asserted that there was a question of fact regarding Stern's credibility and his intent with respect to the transfer (TA at 376-96)

The bankruptcy court did not address any of the issues raised by the parties. Instead, relying on *Wudrick v Clements*, 451 F.2d 988 (9th Cir. 1971), the court determined that Stern had a right to plan for his future and that, as a matter of law, there was nothing improper with transferring assets into a exempt retirement fund, even on the eve of bankruptcy (*See generally* TA at 817-84) Thus, regardless of Stern's intent, his transfer of money from the non-exempt IRA to the exempt Plan was not a fraudulent transfer. (*Id.*)

Appellants filed a timely appeal. (TA at 799.)

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[4] Stern asserted that the creditors had no standing to bring the action. (TA at 37-41)

IV.

LEGAL ANALYSIS

The bankruptcy court's grants of summary judgment are reviewed de novo *In re New England Fish Co.*, 749 F 2d 1277, 1280 (9th Cir 1984) The orders granting summary judgment must be reversed if there are "any genuine factual issues that properly can be resolved only by a finder of fact because they may reasonably be resolved in favor of either party" *Anderson v. Liberty Lobby, Inc.*, 477 U S 242, 250 (1986). When the moving party below properly makes and supports a motion for summary judgment, the opposing party may not rest upon mere denials to create a triable issue, but "must set forth *specific facts* showing that there is a genuine issue for trial." *Fed. R. Civ. P.* 56(e) (emphasis added) An issue is genuine if there is evidence produced that would allow a reasonably jury to reach a verdict in favor of the non-moving party *Anderson*, 477 U.S. at 248 A "scintilla of evidence," or evidence that is "merely colorable" or "not significantly probative," is not sufficient to present a genuine issue as to a material fact *United Steelworkers of America v. Phelps Dodge Corp*, 865 F.2d 1539, 1542 (9th Cir), *cert. denied* 493 U.S. 809 (1989) (quoting *Anderson*, 477 U.S. at 249-50, 252). The bankruptcy court's findings of fact are reviewed for clear error. *In Re Trujillo*, 215 B R. 200 (B.A.P. 9th Cir. 1997).

A. Creditors' Standing

In opposition to the Transfer Appeal, Stern asserts that the Creditors do not have standing to bring the fraudulent transfer action Creditors assert that, because Stern has not perfected the standing argument for appeal, this Court need not reach the issue.

Standing is a necessary prerequisite to this Court's jurisdiction *See Lujan v. Defenders of Wildlife* 504 U.S. 555, 559-60, 112 S. Ct. 2130, 119 L. Ed 2d 351 (1992) (standing is an "essential and unchanging part" of Article III's case-or-controversy requirement). Thus, the Court must address the standing issue even if not addressed by the court below. *See In Re Parmetex, Inc* 199 F.3d 1029, 1030 (9th Cir. 1999) (addressing standing issue even though neither bankruptcy court nor district court addressed issue)

Generally, only the trustee may file an avoidance action in a Chapter 7 bankruptcy. *See Parmetex*, 199 F.3d at 1031. However, the trustee's "exclusive" power to commence such actions is not mandatory. *In Re Curry and Sorensen*, 57 B R 824, 828 (B.A.P. 9th Cir. 1986). Thus, under certain circumstances, creditors may bring avoidance actions *Parmetex*, 199 F.3d at 1031.

A prerequisite to a creditor action is permission from the bankruptcy court *See id.* Here, there is no evidence that Creditors sought the court's approval to bring the transfer action. However, the standing issue had been placed before the court on a number of occasions between 1996-1998. (*See* Creditor's Supplement at 8-13 and TA at 12-16.) While the bankruptcy court never ruled on the issue specifically, it allowed the Creditors to remain in and prosecute the action. Thus, the court appears to have constructively approved Creditors' presence in the action. Accordingly, Creditors have standing to appeal the judgment entered against them.

B. The Exclusion/Exemption Appeal

Generally, a bankruptcy estate includes all of the debtor's legal or equitable interests in property at the time the bankruptcy petition is filed 11 U S C. § 541(a) However, there are exceptions. Relevant to the dispute here, a debtor's beneficial interest in a trust that contains a "restriction on the transfer of [the] beneficial interest . that is enforceable under applicable nonbankruptcy law" is excluded from the estate. 11 U.S.C § 541(c)(2) In addition, the right to receive payment under a pension plan (subject to certain conditions) may be exempted from the bankruptcy estate. 11 U S C §§ 522(b)(1) and (d)(10)(E).

Appellants make four arguments why Stern's interest in Plan should not be excluded from estate or exempted from distribution: (1) the Plan was not qualified under ERISA, (2) the Plan is not excludable under California law; (3) the Plan is not exempt under California law, and (4) even if otherwise exempt, the Plan loses its exemption because the funds were fraudulently conveyed from Stern's IRA

1. The Plan Is Not ERISA Qualified

a. ERISA Qualifications

A pension plan that qualifies under ERISA is excluded from the bankruptcy estate. *Patterson v Shumate*, 504 U.S. 753, 112 S. Ct. 2242, 119 L Ed. 2d 519 (1992) Pertinent to the dispute here, to qualify under ERISA, a pension plan must be for the benefit of "employees." 29 U.S.C. § 1002(2) In addition, the plan must contain an anti-alienation provision. 29 U.S.C. § 1056(d)(1) There is no debate that the Plan here has an anti-alienation provision. (*See* TA at 296).

b. The Plan fails meet the ERISA Requirements Regarding Employees

The purpose of ERISA is to ensure the proper administration of pension plans and to provide protection against abuses by employers whose duty is to manage the pension plan assets for "'workers in traditional employer-employee relationships'" *In Re Lowenschuss*, 171 F 3d 673, 680 (9th Cir), *cert denied* ___ U S ___, 120 S. Ct. 185, 145 L Ed 2d 156 (1999) (citing 29 U.S.C. § 1001 and quoting *Massachusetts Mut. Life Ins Co. v Russell*, 473 U S 134, 142, 105 S Ct 3085, 87 L Ed 2d 96 (1985)).

There is no debate that when the Plan was established in 1992 it was ERISA qualified with one employee, Ms. Mayersohn. The question is whether the policy became disqualified when Mayersohn married Stern. *See* 29 C.F.R. § 2510 3-3(c)(1) (spouse of the sole-owner of the sponsor of a pension plan is not an "employee") Stern asserts, essentially, that once qualified, the Plan was always qualified (*See* TA at 611 ("I would at least go as far as to say, once qualified, always qualified, at least until those charged with qualifying plans disqualify it.")). Appellants assert that the Court should determine ERISA qualification on the date the bankruptcy action was filed

Stern's "once qualified, always qualified" position has been specifically rejected by the Ninth Circuit:

> Debtor argues that the Pension Plan could lose its ERISA status only if it was terminated pursuant to ERISA. We disagree.

Lowenschuss, 171 F.3d at 680 Instead, the question to be addressed is whether, *as of the date the petition for bankruptcy is filed*, the debtor could have enforced the Plan's

transfer restriction *Id*[5] Whether the Plan was once ERISA qualified is not controlling.

Here, the bankruptcy petition was filed in August 1995 – over a year after Stern and Mayersohn were married. The Plan covered no other employees On the date the petition for bankruptcy was filed, the Plan did not satisfy ERISA's requirements that a pension plan "provide retirement income to employees[,]" 29 U S C. § 1002(2)(A)(i), and thus did not qualify under ERISA because the plan was not ERISA qualified, Stern could not use the ERISA laws to enforce the anti-alienation provision of the Plan. Accordingly, the Plan was not excludable by virtue of ERISA qualification.

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[5] Stern attempts to distinguish *Lowenschuss* in three respects. (1) in this case, Mayersohn was an "employee" participant before the marriage, hence the plan was once qualified under ERISA, (2) the Plan here is qualified for favorable tax treatment, and (3) *Lowenschuss* was not meant to destroy a husband's protection of his retirement assets. (*See* Opp at 17-18). First, Stern makes no principled argument of why, in light of the Ninth Circuit's clear rule that the operative date is the date of petition for bankruptcy, this Court should look to Mayersohn's participation prior to marriage Second, the fact that the plan is qualified for favorable treatment under the tax code is irrelevant because the tax code does not give beneficiaries any substantive rights to enforce an anti-alienation provision *See In Re Moses* 215 B.R. 27, 34 (B A P 9th cir. 1997), *aff'd* 167 F.3d 470 (9th Cir 1999) (plan which is tax qualified, but not ERISA qualified, is not excluded from estate absent other applicable state law), *In Re Witwer*, 148 B R 930, 937 (Bankr C.D Cal. 1992), *aff'd* 163 B R 614 (B.A P 9th Cir 1994) Finally, while Stern is correct that *Lowenschuss* is not authority for the proposition that marriage "destroys the husband's right to continue the protection of his retirement assets," *Lowenschuss* also does not hold that when the *sole owner* of a plan sponsor marries the organization's *only employee*, the plan could lose its ERISA status only if formally disqualified

c. Peterson Does Not Change This Result

Stern cites to *Peterson v American Life & Health Ins. Co.*, 48 F 3d 404 (9th Cir.), *cert. denied* 516 U.S. 942, 116 S. Ct. 377, 133 L Ed. 2d 301 (1995), as authority for the once qualified, always qualified rule. In that case, Peterson was a partner in Quivira Marine Service Center ("Quivira"). 48 F. 3d at 405. Quivira sponsored an employee health insurance policy through American Life and Health Insurance Company ("American Policy") for Peterson, his partner and an employee. *Id* The partner and the employee were later covered by a different policy for which Peterson was not qualified, and Peterson remained the only participant in the American Policy *Id.* The question before the Ninth Circuit was whether the American Policy qualified as an ERISA "employee welfare benefit plan" since it did not cover any "employees."

The Ninth Circuit held that the American Policy was part of an overall employee benefit plan that, taken as a whole, was ERISA qualified. *Id.* at 407. The Court further held that, because the American Policy "originally covered a non-partner employee," it remained ERISA qualified. *Id* at 408. Stern relies on the latter holding as support for the "once qualified, always qualified" position

Peterson is not applicable here because that case involved an employee welfare benefit plan, not a pension plan That distinction is important because a welfare benefit plan is ERISA qualified if it "*was established* or maintained for the purpose of providing [benefits] for its participants or

their beneficiaries[.]" 29 U.S.C. § 1002(1)(emphasis added).[6] Thus, an employer's intent in establishing the welfare benefit plan is not only relevant, but may be determinative of ERISA qualification. *See Peterson*, 48 F.3d at 408.

Conversely, pension plans under ERISA do not look to the employer's intent in establishing the plan. Instead, an employee pension benefit qualifies under ERISA "to the extent that by its express terms *or as a result of surrounding circumstances* [the plan] provides retirement income to *employees*, or . . results in a deferral of income by *employees* . . . " 29 U.S.C. § 1002(2)(A) (emphasis added) Thus, by its very terms, ERISA contemplates that circumstances may change and that a pension plan remains qualified only so long as it provides benefits to *employees*. Thus, the plain terms of ERISA distinguishes this case from *Peterson*.[7]

d. The Anti-Alienation Clause is not Sufficient to Make the Plan ERISA Qualified

Finally, Stern cites *In Re Reuter*, 11 F 3d 850 (9th Cir. 1993) for the proposition that the Court should determine ERISA qualification solely by the Plan's anti-alienation provision. *Id* at 852 ("court need look no further than whether the ERISA qualified plan at issue has an anti-alienation provision that satisfies the literal terms" of

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[6] Pension plans are specifically excluded from this definition 29 U S C § 1002(1)

[7] A textual analysis of ERISA is appropriate in bankruptcy cases *See Shumate*, 504 U S at 757, 112 S Ct at 2246 ("the plain language of the Bankruptcy Code of ERISA is our determinant")

Bankruptcy Code). However, *Reuter* is not applicable here. In that case, there was no doubt that the sponsor of the plan – UPS – had "employees;" thus, the plan at issue was ERISA qualified. The only remaining issue regarded the plan's anti-alienation provision. The case does not support Stern's argument that a pension plan can fail to meet ERISA qualifications and still be enforced by the statute Because the Plan here does not have an anti-alienation provision enforceable under ERISA, it is not excludable as an ERISA-qualified plan

2. The Plan is Not Excludable Under State Law

If a plan is not ERISA qualified, it is only excludable from the bankruptcy estate if its anti-alienation provision is enforceable under state law *In Re Moses* 215 B.R. 27, 34 (B.A.P. 9th Cir. 1997) ("*Moses I*"), *aff'd* 167 F 3d 470 (9th Cir. 1999) ("*Moses II*"). California recognizes that excludability of plans containing anti-alienation provisions under statutes and case law governing spendthrift trusts *Moses II*, 167 F 3d at 473; *see generally Cal. Probate Code* §§ 15300 *et seq.* However, if the settlor of such a trust is also a beneficiary of the trust created by him or her ("self-settled trust"), restraints on alienation will not be enforceable as against creditors *Cal Probate Code* § 15304(a).[8]

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[8] The purpose of the prohibition is self-settled trusts is to prevent individuals from getting the benefit of their property while simultaneously placing their property beyond their creditors' reach. *Moses II*, 167 F 3d at 473.

a. Prohibition Against Self-Settled Spendthrift Trusts is Applicable to Pension Plans

Some courts have suggested that this prohibition against self-settled trusts does not apply to pension plans because pension trusts are excluded from the definition of "trust." *See Cal. Probate Code* § 82(b)(13), *see also Moses I*, 215 B.R at 36. However, Section 82 was not meant to insulate pension plans from Section 15304(a)'s prohibition against self-settled trusts. *See Cal Probate Code* 15003(c) The comment to Section 15003(c) clarifies that the provisions of the Trust Law (*i.e. Cal Probate Code* § 15000 et seq) are applicable even to trusts that are excluded under Section 82. *See Cal. Probate Code* § 15003 cmt. ("[s]ubdivision (c) is included to avoid the implication that the provisions of the Trust Law cannot be applied to entities and relationships that are excluded from the definition of 'trust'"). Indeed, given California's strong public policy against self-settled spendthrift trusts, it makes sense to apply the prohibition against pension plans. *In Re Kuraishi*, 237 B.R. 172, 175-76 (C.D. Cal. 1999).

b. The Plan is a Self-Settled Trust

To determine whether a trust is self-settled, the Court looks to the amount of dominion and control exercised by the debtor over the trust property *Moses I*, 215 B.R. 35 [9]

[9] Stern asserts that dominion and control test does not control excludability Opp at 24 (citing *In Re Connor*, 73 F 3d 258 (9th Cir 1995), *cert denied* 519 U.S. 817, 117 S Ct 68, 136, L Ed 2d 29 (1996)) In *Conner*, the Court rejected the "dominion and control" test when

(Continued on following page)

This inquiry is one of fact and, as the bankruptcy court noted, "the record with regard to dominion and control [is] skimpy in this case [ ]" *See* TA2 at 654. Nevertheless, the bankruptcy court concluded that the record showed that Stern had too much control over the funds to permit enforcement of the anti-alienation provision. This Court agrees.

Stern is the sole shareholder and owner of the corporate sponsor of the Plan, Stern, Inc. He is the trustee and the majority beneficiary.[10] (TA2 at 328) While only Stern, Inc could terminate the Plan, Stern was a member of Stern, Inc's Board of Directors (*See* TA2 at 220, 224-25, 291.) Finally, as trustee, Stern had discretion to make loans to participants (TA2 at 284) Thus, Stern exercises sufficient control to prevent the plan from qualifying as a spendthrift trust. *See In Re Kaplan* 97 B.R. 572 (B A P. 9th Cir 1989); *cf Moses I*, 215 B R. at 36 (pension plan excludable where debtor participated in plan sponsored by large employer and (1) debtor lacked ability to terminate or amend plan individually, (2) his participation was

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determining the excludability of ERISA plans because, in determining whether to exclude ERISA plans from bankruptcy estates, "the Supreme Court appears to have discounted any distinctions based on the debtors' control of their assets" *Id.* at 259 Stern asserts that there is no principled difference between ERISA and state law

To the contrary, there is a principled difference. As discussed above, ERISA plans are established by employers for their employees By definition, ERISA-qualified plans are not self-settled and thus there are not the same public policy concerns regarding alienation. *See* n 8, *supra Conner* therefore does not change the "dominion and control" plan for non-ERISA qualified plans

[10] In February 1998, Stern's interest in the plan was $2,100,000 and Margaret Stern's interest was $9,300 (TA2 at 328)

irrevocable; (3) his contributions were determined by Tax Code and were not optional, (4) debtor could not receive funds but for retirement, disability or termination of employment, and (5) debtor could not take loans against plan); *cf also In Re Kincaid*, 917 F.2d 1162 (9th Cir. 1990) (pension plan was excludable because (1) plan was not created or administered by debtor; (2) debtor could only withdraw interest under certain limited conditions; and (3) access to funds was only through administrator).

Thus, the Plan is not excludable under California law.

The Plan is Entirely Exempt Under California Law

Because the Plan is not excludable from the bankruptcy estate, the Court next determines if it is exempt from distribution to creditors *See Moses II*, 167 F.3d at 474 ("exemption issues arise only if court concludes that the Plan is part of the bankruptcy estate"); 11 U.S.C § 522 Under the Bankruptcy Code, a debtor may choose to apply either federal or state exemption law, 11 U.S.C. § 522(b) Here, Stern has chosen to apply California law

Under California law, funds held in private retirement plans are exempt from distribution *Cal. Civ. Proc. Code* § 704 115(b) A "private retirement plan" includes (1) private retirement plans (*Cal. Civ Proc Code* § 704 115(a)(1)), (2) profit-sharing plans "designed and used for retirement purposes" (*Cal. Civ. Proc Code* § 704.115(a)(2)), and (3) self-employed retirement plans and individual retirement annuities (*Cal Civ Proc. Code* § 704.115(a)(3)). The distinction between the (a)(1) and (a)(2) plans on the one hand, and (a)(3) plans on the other, is important private retirement plans and profit sharing plans are entirely exempt from distribution, whereas IRAs are

exempt "only to the extent necessary to provide for the support" of the debtor. *Cal Civ Proc Code* § 704.115(e).

Here, although the Plan provides mostly for Stern alone, it is a corporate plan entitled to total exemption under either (a)(1) or (a)(2) [11] At the time it was established, the Plan was made up entirely of money specifically designated for retirement purposes [12] Appellants do not dispute the source of the funds. However, Appellants assert that, if the Plan is exempt at all (see below), it is at most entitled to limited exemption under (a)(3) as a self-employed retirement plan.

This argument fails because the plan is sponsored by Stern, Inc , the corporation, and not Steven H. Stern, the individual. Corporate plans, no matter how closely held, are entitled to complete exemption. *In re Cheng*, 943 F.2d 1114, 1116 (9th Cir 1991) (plan sponsored by corporation whose sole shareholder, president and controlling executive was debtor was nevertheless entitled to complete exemption).[13]

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[11] Because the distinction between (a)(1) and (a)(2) is not at issue here, the Court makes no determination as to which of the categories this plan falls

[12] This is not destroyed simply because Stern took out a loan against the Plan *See In Re Bloom*, 839 F 2d 1376, 1379 (9th Cir 1988) (key question is whether plan is used for retirement purposes, loans pursuant to plan documents are not so abusive as to change purpose of retirement plan).

[13] Appellants assert that the *Cheng* case has been contradicted by *In Re Mooney*, 248 B R 391 (Bankr 2000). *Mooney* faced the opposite question of that presented here, the status of assets that were formerly part of a pension plan, but part of an IRA at the time of bankruptcy There was no dispute that (a)(3) applied

Thus, Stern's interest in the plan is exempt from distribution.[14]

4. The "Fraudulent Conveyance" Does Not Destroy Exemption

Appellants finally argue that the Court should not exempt Stern's interest in the Plan because Stern "fraudulently conveyed" the corpus This argument raises the same issues as the Transfer Appeal. For the reasons discussed below, the Court finds that the transfer was not "fraudulent." *Wudrick v. Clements*, 451 F 2d 988, 989-90 (9th Cir 1971); *see In Re Moffat*, 107 B.R. 255, 266 (Bankr C D. Cal. 1989), *aff'd* 119 B.R. 201 (B.A.P. 9th Cir. 1990) *aff'd* 959 F 2d 740 (9th Cir. 1992). Thus Stern's interest in the Plan assets is exempt

C. The Transfer Appeal

The issue on the Transfer Appeal is whether the assets that were once part of Stern's IRA can be reached

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[14] Appellants assert that, even if the corpus of the Plan was exempt before the transfer, it lost its exempt status when transferred *See, eg., In Re Trujillo* 215 B R 200 (B.A P. 9th Cir 1997), *aff'd* 166 F 3d 1218 (9th Cir. 1998) (holding that "[s]ince the Debtors had voluntarily transferred their property, they were no longer entitled to the exemption") However, in *Trujillo*, debtors transferred assets in a manner inconsistent with the policies permitting exemption, that is, debtors transferred their house and other property to third parties Debtors were not entitled to simply "reverse" the transaction when beneficial to them Here, in contrast, Stern's transfer was consistent with the policies regarding exemption – he transferred the money from one exempt plan to another Holding that such transfer makes the assets non-exempt would be contrary to the Ninth Circuit's holding in *Wudrick, supra*

by Stern's creditors. Under California law, a transfer may be avoided if it was made with "actual intent to hinder, delay, or defraud any creditor" or if it was made "[w]ithout receiving a reasonably equivalent value in exchange " *Cal Civ Code* §§ 3439 04 and 3439 06

The parties' primary dispute is whether the movement of the money from the IRA to the Plan constituted a "transfer." The Court need not decide this issue because, even if it assumes Appellants' position that there was a transfer, Stern is still entitled to summary judgment [15] Thus, in the proceedings below, the bankruptcy court assumed that Stern transferred the money from his IRA to the Plan with the intent of placing the money outside the reach of his creditors. Relying on case law holding that pre-bankruptcy planning is not evidence of fraud, the court granted Stern's motion for summary judgment.

1. Summary Judgment Was Properly Granted as to the Constructive Fraud Claims (Fifth and Sixth Causes of Action)

Under the California Civil code, a transfer is fraudulent if it is made without receiving a reasonably equivalent

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[15] The Court notes that Appellants' position has legal support Both the Bankruptcy Code and the California Civil Code define "transfer" broadly 11 U S C § 101(54), *Cal Civ Code* § 3439 01(i); *see In Re Bernard*, 96 F 3d 1279, 1282 (9th Cir 1996) (definition of transfer is "extremely broad"). "Transfer" includes transfer of possession, custody, or control, even if there is no transfer of title *Bernard*, 96 F 3d at 1282 (quoting the Senate Report on Section 101(54)). Here, the money was "transferred" from an individual account to a corporate plan, thus, transferring possession custody and control *See id* (withdrawing money from bank account considered "transfer")

value. *Cal Civil Code* §§ 3439.04(b) and 3439 05. The debtor's intent is immaterial. *See In Re Cohen*, 199 B.R. 709, 717 (B.A P. 9th Cir. 1996). What is a "reasonably equivalent value" is assessed from the perspective of the creditors *In Re Prejean*, 994 F 2d 706, 709 (9th Cir. 1993). Appellants argue that by transferring non-exempt property into exempt property, Stern did not receive equivalent value (*i e* the value to the creditors fell from approximately $1 4 million to $0) and thus the transfer should be avoided.

This argument has been squarely rejected by the Ninth Circuit The Court has held that the purposeful conversion of nonexempt property into exempt assets on the eve of bankruptcy is not per se fraud. *Wudrick*, 451 F 2d at 989-90; *See In Re Moffat*, 107 B.R. 255, 266 (Bankr. C.D. Cal 1989) To hold otherwise would penalize debtors for using entitlements granted under the bankruptcy laws. *See In Re Smiley*, 865 F.2d 562, 566 (7th Cir. 1989)(citing House and Senate Reports). Because Appellants have not provided any evidence of constructive fraud beyond the mere transfer of assets, the bankruptcy court properly granted summary judgment on the Fifth and Sixth Causes of Action. *See Kuptez v. Wolf*, 845 F 2d 842, 848 (9th Cir. 1998) ("we hesitate to utilize constructive intent to frustrate the purposes intended to be served by what appears to us to be a legitimate [transaction]")

Summary Judgment Was Properly Granted As to the Actual Fraud Claim (Fourth Cause of Action)

While transferring nonexempt assets to exempt assets is not per se fraud, such a transfer is avoidable where the debtor's conduct in converting his or her assets rises to the

level of actual fraud. *In Re Moffat*, 107 B.R. at 266. The bankruptcy court did not reach the issue of whether Stern's actions rose to the level of actual fraud.

In determining whether Stern's actions rose to the level of fraud, courts may look to circumstantial evidence as "badges of fraud." *Kuptez*, 845 F.2d at 846 Appellants point to five badges of fraud (1) Stern was sued before the transfer, (2) Stern's insolvency before making the transfer; (3) the transfer occurred shortly after a substantial debt was incurred; (4) Stern retained control and possession of the property, (5) the proportion of Stern's assets transferred (Opening Brief at 14-15.) Appellants also raise issues of Stern's credibility and his contemporaneous divorce. (*Id*)

a. The Badges of Fraud Do Not Lead to a Showing of Fraud

The existence of one or more badges of fraud does not create a *presumption* of fraud. *See Cal. Civ. Code* § 3439 04 cmt. 5. In considering the badges, a court must also consider the factors that negate a finding of fraud *Cal Civ Code* § 3439 04 cmt. 7

Here, the first three badges amount to nothing more than an argument that, because Stern transferred the funds on the eve of bankruptcy, he had a fraudulent intent As discussed above, such transfers are permitted under the Bankruptcy Code and thus are not evidence of fraud

The fourth badge, Stern's continued control of the property, also does not evidence fraud here. Retention of possession and control indicates fraud when debtors

misrepresent the value of their assets by deceiving creditors into believing they actually own the property when, in reality, title transferred to a third party *See Smiley*, 864 F 2d at 568 (debtor misrepresented value of assets by telling creditors that assets included full value of a house that had actually been deeded to daughter). Here, Stern openly disclosed the transfer; therefore, creditors were not led to believe Stern owned something he did not. Thus, the fact that he retained possession and control does not evidence fraud.

Finally, Appellants do not present evidence regarding the proportion of assets represented by the transfer or show how this constitutes an indication of fraud.

b. Stern's Credibility Is Not At Issue

Appellants assert that a trial is necessary to assess Stern's credibility because his 1998 declaration regarding his good faith in making the transfer is allegedly belied by his earlier 1992 and 1994 depositions "in which he recalled little about the transfer" (Appellants' Opening Brief at 14.) Appellants fail to show how Stern's intentions with respect to the transfer alter the outcome It is undisputed that the transferred money had always been set aside for Stern's retirement *See* SUF 1-13, TA at 365-67, *see also* TA at 846 ("no one disputes [the money] has always been held for retirement purposes"), *cf In Re Phillips*, 218 B R. 520, 523 (N.D. Cal. 1998)(finding no exemption where "retirement" accounts were not actually "designed and used" for retirement purposes). Thus, whether Stern transferred the money for the reasons stated or with the express purpose to keep the money out of his creditors' reach is irrelevant.

Either way, the money remains exempt *See Wudrick*, 451 F.2d 988

c. Stern's "Uncontested and Sudden" Divorce Does Not Show Fraud

Appellants suggest that Stern's divorce is evidence of fraud because it was "uncontested and sudden," the division of property was without appraisals, and Sharma Stern's attorney "clearly [took] the direction and lead of Stern's attorney both procedurally and substantively" (Appellants' Opening Brief at 15.) This entire argument is unsupported in fact and law.

First, there is no evidence that the divorce was "sudden" Appellants do not contest that the Sterns' marriage problems dated back in August 1990, that the Sterns agreed to separate in 1991, and that Stern contacted a divorce attorney in May 1992 These events all occurred before the arbitration award issued. Moreover, there is no evidence that divorce is a sham as suggested by Trustee *See* TA at 822; *see also* SUF 17(Stern remarried in 1994).

Second, with respect to the quality of divorce attorneys, there is no evidence in the record that Sharma Stern's attorney was not acting independently.

Finally, while the law of fraudulent conveyances applies to transfers between married spouses, it does not apply to transfers as part of a dissolution proceeding *Gagan v. Gouyd*, 73 Cal App 4th 835, 842-43, 86 Cal Rptr 2d 733, 737 (1999). Thus, Appellants' bald statements regarding the failure to appraise the property as part of the dissolution proceedings fails to raise a genuine issue of fact sufficient to reverse summary judgment.

d. Stern Did Not Hinder or Delay

Finally, while a transfer may be "fraudulent" if it merely "hinders or delays" a debtor's creditors, *see Cal. Civ Code* § 3439.04, the record is devoid of any evidence that Stern hindered or delayed his creditors beyond that which he was legally entitled to do under *Wudrick*. *Cf. Simley*, 864 F 2d at 568 (debtor's actions in failing to tell creditors he converted assets was not fraud; but transfer was avoidable because debtor intended to hinder and delay creditors from filing bankruptcy until he could establish residency in another state to take advantage of that state's exemption laws).

V.

CONCLUSION AND ORDER

Stern's interest in the Plan is not excluded from the bankruptcy estate because it does not have an anti-alienation provision that is enforceable by non-bankruptcy law However, the Plan assets are exempted from distribution because the Plan is a profit sharing plan "designed and used" for retirement purposes. There is no finding of "fraudulent transfer" that would change this status or would allow Appellants to avoid the transfer Accordingly, the order granting Stern's Motion for Summary Judgment Re Pension Plan Interests and order granting Stern's Exclusion/Exemption Motion for Summary Judgment are AFFIRMED.

IT IS SO ORDERED.

DATED: July 27, 2000

/s/ Gary Feess
Judge Gary Allen Feess
United States District Court

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UNITED STATES BANKRUPTCY COURT

CENTRAL DISTRICT OF CALIFORNIA

In re	) bk. No. SV 95-16165-KL
STEVEN H. STERN,	) [Chapter 7 Case]
Debtor.	) Adv. No. SV 95-01544-KL
DOVE AUDIO, INC.; MICHAEL VINER; JERRY LEIDER;	) FOURTH AMENDED COMPLAINT TO AVOID FRAUDULENT TRANSFERS AND TO RECOVER GENERAL AND PUNITIVE DAMAGES
Plaintiffs,	)
DAVID A. GILL, as Trustee;	) (Filed Feb. 12, 1997)
Plaintiff in Intervention,	) Date: SEE SUMMONS
v.	) Time: SEE SUMMONS
	) Place: SEE SUMMONS

STEVEN H. STERN, individually and as trustee for The Steven H. Stern, Inc. Profit Sharing Plan; SHARMA STERN; SHARMHILL PRODUCTIONS, INC., an Ontario (Canada) Corporation; STEVEN H. STERN, INC.; CANDICE MADNICK; TODD MADNICK; THE STEVEN H. STERN INC. PROFIT SHARING PLAN; Defendants.

Plaintiffs allege:

GENERAL ALLEGATIONS

1. The jurisdiction of this Court is invoked under 28 U.S.C. Section 1334(b). Venue is proper in this Court pursuant to 28 U.S.C. Section 1409(a)(c). This Adversary Proceeding arises in, and relates to, the Chapter 7 Case for Steven H. Stern, as debtor (the "debtor" or "Steven"), pending in the United states Bankruptcy Court for the Central District of California, San Fernando Valley Division, which is designated therein as Case No. SV-95-16165-KL (the "Chapter 7 Case"). The Chapter 7 Case was commenced by an original, voluntary petition filed on August 11, 1995 (the "Petition Date"). This adversary proceeding is a core proceeding within the meaning of 28 U.S.C. Section 157(b).

2. The Plaintiff in Intervention is David A. Gill, in his capacity as the Trustee serving in the Chapter 7 Case (the "Trustee").

3. The Plaintiffs Dove Audio, Inc. ("Dove"), Michael Viner ("Viner") and Jerry Leider ("Leider") are, and were at all relevant times, creditors of the Defendant Steven H. Stern.

4. Dove, Viner and Leider are referred to in this Complaint, jointly and severally, as, "Dove Audio". The Trustee, Dove, Viner and Leider are referred to in this Complaint, jointly and severally, as, the "Plaintiffs".

5. The Defendant Steven H. Stern is an individual and the debtor in the Chapter 7 Case, who is named and sued herein both in his individual capacity and as the trustee of Defendant The Steven H. Stern, Inc. Profit Sharing Plan (the "SHS Plan") and he will be referred to in this Complaint, in each and both of such capacities, as, "Steven".

6. The Plaintiffs are informed and believe and, based thereon, allege that the defendant The Steven H. Stern, Inc. Profit Sharing Plan (the "SHS Plan") purports to be an employee benefit plan, formed in or about October of 1992 through the use of back dated documents.

7. The Defendant Sharmhill Productions, Inc. ("Sharmhill") purports to be a corporation organized under the laws of the Province of Ontario, Canada.

8. The Defendant Steven H. Stern, Inc. ("SHS Inc.") purports to be a corporation.

9. The Defendant Sharma Stern ("Sharma") is an individual person whose present residence is unknown.

The Plaintiffs are informed and believe and based thereon allege that Sharma was a resident of Los Angeles, California at all times relevant herein, and that she has appeared in this Adversary Proceeding.

10. The Plaintiffs are informed and believe and, based thereon, allege that Defendant Candice Madnick ("Candice") is the daughter of Steven and Sharma, and Todd Madnick ("Todd") was their son-in-law at all times relevant herein. Candice and Todd are referred to in this Complaint jointly and severally as the "Madnicks". The Plaintiffs are further informed and believe and, based thereon, allege that the Defendant Madnicks were residents of Los Angeles, California all times relevant herein.

11. Steven, Sharma, the Madnicks, the SHS Plan, Sharmhill and SHS Inc. are referred to in this Complaint, jointly and severally, as, the "Defendants".

12. As among themselves, the Plaintiffs reserve all of their rights and interests with respect to the claims alleged in this Complaint as against the Defendants, as well as with respect to any recovery upon such claims.

13. The Plaintiffs are informed and believe and, based thereon, allege that, at all relevant times, there existed a unity of interest and ownership between and among the Defendant Steven, and the Defendants Sharmhill, SHS Inc. and the SHS Plan, who purport to be corporations or other entities, such that any individuality or separateness between the Defendant Steven, on the one hand, and the Defendants, Sharmhill, SHS Inc. and the SHS Plan, on the other hand, has ceased or never existed.

14. The Plaintiffs are further informed and believe and, based thereon, allege that the Defendants Sharmhill,

SHS Inc. and the SHS Plan are and were, at all relevant times, mere shells, instrumentalities and conduits through which the Defendant Steven carried on, and carries on, his financial affairs and hides assets from his creditors.

15. The Plaintiffs are further informed and believe and, based thereon, allege that the adherence to a fiction of the separate existence of defendants Sharmhill, SHS Inc. and/or the SHS Plan, as entities distinct from Defendant Steven, would permit an abuse of a corporate or limited liability privilege and would sanction a fraud and promote injustice.

16. The Plaintiffs are informed and believe and, based thereon, allege that each of the defendants named and sued herein, in doing the things and failing to do the things complained of herein, acted as the agent and employee of the remaining Defendants, within the course and scope of such agency and employment, such that any action or failure to act complained of herein by one Defendant was done for the benefit of, and is chargeable to each and all of the other Defendants.

17. This adversary proceeding originated from the commencement of that certain action known as *Dove Audio, Michael Viner and Jerry Leider v. Steven Stern, et al.,* Case No. BC 072892 before the Los Angeles Superior Court (the "State Court Action"), which action was properly removed to this court pursuant to 28 U.S.C. section 1452.

18. In September, 1992, Dove Audio obtained an arbitration award for $4,585,000.00 which was confirmed and became a final judgment for an amount in excess of $4,700,000.00 as against the Defendant Steven and as against another of defendant Steven's corporations,

Sharmhill Productions, Inc. of British Columbia, Canada (the "Arbitration Award"), which award included a finding that Sharmhill Productions, Inc. of British Columbia, Canada was an alter ego of Defendant Steven.

19. The Plaintiffs are informed and believe and, based thereon, allege that in response to the litigation leading to the Arbitration Award and following the issuance of the Arbitration Award, the Defendants with other named and unnamed coconspirators implemented a scheme to transfer substantially all of Steven's valuable non-exempt assets in an attempt to place such assets beyond the reach of his creditors.

20. The Plaintiffs are informed and believe and, based thereon, allege that in furtherance of this fraudulent scheme, in or about October, 1992, Steven and Sharma conspired with each other and other unnamed coconspirators to enter into and did enter into a marital settlement agreement (the "MSA"), pursuant to which Steven transferred many of his valuable, non-exempt assets in an attempt to place such assets beyond the reach of his creditors.

21. The Plaintiffs are informed and believe and, based thereon, allege that in or about October of 1992, the Defendant Steven transferred certain assets (jointly and severally, the "Sharma Transfer Assets") to Sharma (jointly and severally, the "Sharma Transfers"), including the following:

(a) $190,000 in cash derived from the Defendant Steven closing various accounts at the Bank of America on or about October 13, 1992;

(b) $200,000 in cash derived from Defendant Steven's account at the Bank of Nova Scotia on or about October 19, 1992;

(c) $225,000 in cash derived from Defendant Steven's account at First Interstate Bank on or about October 19, 1992;

(d) $110,000 in cash derived from Defendant Steven's escrow account at Escrow Consultants on or about October 19, 1992;

(e) A receivable in the approximate amount of $116,000 due from SHS, Inc. to Defendant Steven in or about October, 1992;

(f) all of the Defendant Steven's interest in the real property commonly known as, 4321 Clear Valley Drive, Encino, California on or about October 23, 1992;

(g) $287,103 in assets which were derived from the Defendant Steven's then existing non-exempt personal IRA account.

(h) Steven's community interest in that certain condominium located at 4350 Stern Avenue, Unit 12, Sherman Oaks, California, 91423 (the "Madnick Condominium").

(i) properties and interests in properties transferred to the Defendant Sharma by the Defendant Steven in or about October of 1992 disguised in the form of the MSA.

22. The Plaintiffs are informed and believe, and based thereon, allege that the Madnicks resided at the Madnick Condominium prior to the date of the Arbitration Award, and continued to reside at said property after the date of the transfer of Steven's community interest in the

property to Sharma. The Plaintiffs are informed and believe, and based thereon, further allege that Sharma received the transfer of Steven's community interest in the Madnick Condominium for and on account of the exclusive benefit of the Madnicks, that Sharma took title to the Madnick Condominium in furtherance of a conspiracy between Steven, Sharma and the Madnicks to place Steven's community interest in the Madnick Condominium beyond the reach of creditors of Steven, and that this scheme was implemented by the Defendants Steven, Sharma and the Madnicks with the specific intent to hinder, delay and to defraud creditors of the Debtor for the benefit of the Madnicks.

23. The Plaintiffs are informed and believe, and based thereon, allege that in or about October, 1992, Steven signed a resolution of the Board of Directors of SHS, Inc. establishing the SHS Plan. The Plaintiffs are informed and believe, and based thereon, allege that in or about October, 1992, the Defendant Steven transferred approximately $1,400,000 from a non-exempt personal IRA account to the SHS Plan (the "IRA Transfer").

FIRST CLAIM FOR RELIEF

[Claim of the Plaintiffs Against Sharma and the Madnicks to Avoid Fraudulent Transfers

[Cal. Civ. Code §3439.04(a)]

24. The Plaintiffs refer to and, by this reference, incorporate and allege herein each and all of the allegations set forth in Paragraphs 1 through 23, inclusive, of this Complaint.

25. The Plaintiffs are informed and believe and, based thereon, allege that in or about October of 1992, the Debtor made the Sharma Transfers with the specific and actual intent to hinder, delay and defraud creditors of the Debtor.

26. The Plaintiffs are informed and believe and, based thereon, allege that, pursuant to 11 U.S.C. section 544(b) and California Civil Code section 3439.04(a), the Plaintiffs may avoid the Sharma Transfers, and recover the Sharma Transfer Assets or, at the option of the Plaintiffs, obtain a money judgment against Defendant Sharma for the value of the Sharma Transfer Assets as of the date of the Sharma Transfers.

27. The Plaintiffs are informed and believe and, based thereon, further allege that, pursuant to 11 U.S.C. section 544(b) and California Civil Code section 3439.04(a), the Plaintiffs may avoid the transfer of the Debtor's interest in the Madnick Condominium and, at the option of the Plaintiffs, obtain a money judgment against Defendants Sharma and the Madnicks for the value of the Debtor's interest in the Madnick Condominium as of the date of the Debtor's transfer of such interest.

SECOND CLAIM FOR RELIEF

[Claim of the Plaintiffs Against Sharma and the Madnicks to Avoid Fraudulent Transfers]

[Cal. Civ. Code §3439.04(b)(1)-(2)]

28. The Plaintiffs refer to and, by this reference, incorporate and allege herein each and all of the allegations set forth in Paragraphs 1 through 27, inclusive, of this Complaint.

29. The Plaintiffs are informed and believe and, based thereon, allege that the Defendant Steven did not receive reasonably equivalent value in exchange for the Sharma Transfers.

30. The Plaintiffs are informed and believe and, based thereon, allege that the Sharma Transfers were made while the Defendant Steven was engaged or was about to engage in a business or transaction for which his remaining assets were unreasonably small in relation to such business or transactions.

31. The Plaintiffs are informed and believe and, based thereon, allege that the Sharma Transfers were made at a time when the Defendant Steven intended to incur, or believed, or reasonably should have believed, that he would incur debts beyond his ability to pay such debts as they became due.

32. The Plaintiffs are informed and believe and, based thereon, allege that the Defendant Steven was insolvent at the time of the Sharma Transfers, or that the Defendant Steven became insolvent as a result of the Sharma Transfers.

33. The Plaintiffs are informed and believe and, based thereon, allege that, pursuant to pursuant to 11 U.S.C. section 544(b) and California Civil Code section 3439.04(b), the Plaintiffs may avoid the Sharma Transfers, and recover the Sharma Transfer Assets or, at the option of the Plaintiffs, obtain a money judgment against the Defendant Sharma for the value of the Sharma Transfer Assets as of the date of the Sharma Transfers.

34. The Plaintiffs are informed and believe and, based thereon, further allege that, pursuant to 11 U.S.C. section 544(b) and California Civil Code section 3439.04(b), the Plaintiffs may avoid the transfer of the debtor's interest in the Madnick Condominium and, at the option of the Plaintiffs, obtain a money judgment against Defendants Sharma and the Madnicks for the value of the Debtor's interest in the Madnick Condominium as of the date of the Debtor's transfer of such interest.

THIRD CLAIM FOR RELIEF

[Claim of Plaintiffs Against Sharma and the Madnicks to Avoid Fraudulent Transfers]

[Cal. Civ. Code §3439.05]

35. The Plaintiffs refers to and, by this reference, incorporates and alleges herein each and all of the allegations set forth in Paragraphs 1 through 34, inclusive, of this Complaint.

36. The Plaintiffs are informed and believe and based thereon allege that the Defendant Steven was insolvent at the time of the Sharma Transfers, or that the Defendant Steven became insolvent as a result of the Sharma Transfers.

37. The Plaintiffs are informed and believe and, based thereon, allege that the Defendant Steven did not receive reasonably equivalent value in exchange for the Sharma Transfers.

38. The Plaintiffs are informed and believe and, based thereon, allege that, pursuant to pursuant to 11 U.S.C. section 544(b) and California Civil Code section

3439.05, the Plaintiffs may avoid the fraudulent transfers made to Sharma, which are included in the Subject Transfers, and recover the properties fraudulently transferred or, at the option of the Plaintiffs, obtain a money judgment against Defendant Sharma for the value of the properties fraudulently transferred as of the date of the fraudulent transfers.

39. The Plaintiffs are informed and believe and, based thereon, further allege that, pursuant to 11 U.S.C. section 544(b) and California Civil Code section 3439.04(b), the Plaintiffs may avoid the transfer of the Debtor's interest in the Madnick Condominium and, at the option of the Plaintiffs, obtain a money judgment against Defendants Sharma and the Madnicks for the value of the Debtor's interest in the Madnick Condominium as of the date of the Debtor's transfer of such interest.

FOURTH CLAIM FOR RELIEF

[Claim of Plaintiffs Against the Defendants Steven And The SHS Plan To Avoid Fraudulent Transfers]

[Cal. Civ. Code §3439.04(a)]

40. The Plaintiffs refer to and, by this reference, incorporate and allege herein each and all of the allegations set forth in Paragraphs 1 through 39, inclusive, of this Complaint.

41. The Plaintiffs are informed believe, and based thereon, allege that the IRA Transfer was made by the Defendant Steven and the Defendant SHS Plan with the

specific intent to hinder, delay and to defraud creditors of the Debtor.

42. The Plaintiffs are informed and believe and, based thereon, allege that, pursuant to pursuant to 11 U.S.C. section 544(b) and California Civil Code section 3439.04(a), the Plaintiffs may avoid the IRA Transfer and obtain a money judgment against the Defendant Steven and the Defendant SHS Plan for the value of the IRA Funds together with an Order directing the Defendant SHS Plan and the Defendant Steven to deliver such property to the Plaintiffs.

FIFTH CLAIM FOR RELIEF

[Claim of the Plaintiffs Against Defendants Steven and the SHS Plan to Avoid Fraudulent Transfers]

[Cal. Civ. Code §3439.04(b) (1)-(2)]

43. The Plaintiffs refer to and, by this reference, incorporate and allege herein each and all of the allegations set forth in Paragraphs 1 through 42, inclusive, of this Complaint.

44. The Plaintiffs are informed and believe and, based thereon, allege that the Defendant Steven did not receive reasonably equivalent value in exchange for the IRA Transfer.

45. The Plaintiffs are informed and believe and, based thereon, allege that the IRA Transfer was made while the Defendant Steven was engaged or was about to engage in a business or transaction for which his remaining assets were unreasonably small in relation to such business or transactions.

46. The Plaintiffs are informed and believe and, based thereon, allege that the IRA Transfer was made at a time when the Defendant Steven intended to incur, or believed, or reasonably should have believed, that he would incur debts beyond his ability to pay such debts as they became due.

47. The Plaintiffs are informed and believe and, based thereon, allege that the Defendants Steven was insolvent at the time of the IRA Transfers, or that the Defendant Steven became insolvent as a result of the IRA Transfer.

48. The Plaintiffs are informed and believe and, based thereon, allege that, pursuant to pursuant to 11 U.S.C. section 544(b) and California Civil Code section 349.04(b), the Plaintiffs may avoid the IRA Transfer and obtain a money judgment against the Defendant Steven and the Defendant SHS Plan for the value of the IRA Funds together with an Order directing the Defendant SHS Plan and the Defendant Steven to deliver such property to the Plaintiffs.

SIXTH CLAIM FOR RELIEF

[Claim of Plaintiffs Against Sharma and SHS Plan to Avoid Fraudulent Transfers]

[Cal. Civ. Code §3439.05]

49. The Plaintiffs refer to and, by this reference, incorporate and allege herein each and all of the allegations set forth in Paragraphs 1 through 48, inclusive, of this Complaint.

50. The Plaintiffs are informed and believe and based thereon, allege that the Defendant Steven was insolvent at the time of the IRA Transfer, or that the Defendant Steven became insolvent as a result of the IRA Transfer.

51. The Plaintiffs are informed and believe and, based thereon, allege that the Defendant Steven did not receive reasonably equivalent value in exchange for the IRA Transfers.

52. The Plaintiffs are informed and believe and, based thereon allege that the IRA Transfer is fraudulent as to creditors of the Debtor whose claims arose before the IRA Transfer was made.

52. The Plaintiffs are informed and believe and, based thereon, allege that, pursuant to pursuant to 11 U.S.C. section 544(b) and California Civil Code section 3439.04(b), the Plaintiffs may avoid the IRA Transfer and obtain a money judgment against the Defendant Steven and the Defendant SHS Plan for the value of the IRA Funds together with an Order directing the Defendant SHS Plan and the Defendant Steven to deliver such property to the Plaintiffs.

SEVENTH CLAIM FOR RELIEF

[Claim of Plaintiffs Against All Defendants to Recover General and Punitive Damages For Conspiring to Effect Fraudulent Transfers]

54. The Plaintiffs refer to and, by this reference, incorporate and allege herein each and all of the allegations

set forth in Paragraphs 1 through 53, inclusive, of this Complaint.

55. The Plaintiffs are informed and believe and, based thereon, allege that, prior to October of 1992, the Defendants knowingly and intentionally entered into an ongoing fraudulent agreement and conspiracy among themselves and other unnamed co-conspirators to hinder, delay and defraud creditors of the Debtor by means of the Sharma Transfers, the IRA Transfer and other transfers. The Plaintiffs are further informed and believe and, based thereon, allege that said continuing fraudulent conspiracy was uninterrupted and ongoing at the time of the Sharma Transfers and the IRA Transfer as of the commencement of the Chapter 7 Case and as of the filing of this Fourth Amended Complaint.

56. The Plaintiffs are informed and believe and, based thereon, allege that, by reason of said unlawful agreement and fraudulent conspiracy among the Defendants and others, the Plaintiffs are entitled to a money judgment for general damages as against each Defendant conspirator for an amount equal to not less than the total aggregate value of all properties transferred to all other Defendant conspirators, in amounts according to proof.

57. The Plaintiffs are informed and believe and, based thereon, allege that in doing the things complained of herein, the Defendants acted maliciously, with the specific intention of defrauding and damaging creditors of the Debtor, including, Dove Audio, for the pecuniary benefit of the Defendants, so that the Plaintiffs are entitled to a money judgment against the Defendants for punitive damages, in amounts to be determined at trial.

WHEREFORE, the Plaintiffs pray for judgment against the Defendants as follows:

A. **ON THE FIRST, SECOND, AND THIRD CLAIMS FOR RELIEF:**

(1) For Judgment avoiding the Sharma Transfers; or, at the option of the Plaintiffs, in the alternative,

(2) For Judgment for money against the Defendant Sharma in amounts equal to the value of the Sharma Transfer Assets;

(3) For Judgment avoiding the transfer of the Debtor's interest in the Madnick Condominium; or at the option of the Plaintiffs, in the alternative,

(4) For Judgment for money against the Defendants Sharma and the Madnicks in amounts equal to the value of the Madnick Condominium;

B. **ON THE FOURTH, FIFTH, AND SIXTH CLAIMS FOR RELIEF:**

(1) For Judgment avoiding the IRA Transfer; or, at the option of the Plaintiffs, in the alternative,

(2) For Judgment for money against the Defendants Steven and the SHS Plan in amounts equal to the value of the IRA Funds;

C. **ON THE SEVENTH CLAIM FOR RELIEF:**

(1) For Judgment for general damages as against the Defendants in amounts according to proof;

(2) For punitive damages in an amount to be determined at trial; and

(3) For Judgment avoiding the Sharma Transfers and the IRA Transfer; or, at the option of the Plaintiffs, in the alternative,

(4) For Judgment for money against all Defendants in amounts equal to the value of the Sharma Transfer Assets and the IRA Funds;

D. **ON EACH AND ALL OF THE CLAIMS FOR RELIEF:**

(1) For the Plaintiffs' reasonable attorneys' fees and costs of suit incurred herein; and,

(2) For such other and further relief as may be determined just and proper in the premises.

Dated: February 12, 1997 DANNING, GILL, DIAMOND & KOLLITZ, LLP

By /s/ Kevin L. Hing
Kevin L. Hing
Attorneys for Plaintiff in Intervention, David A. Gill, as Trustee

Dated: February 12, 1997 IVERSON, YOAKUM, PAPIANO & HATCH
Andrew K. Doty

(and)

STEINBERG, NUTTER & BRENT, Professional Corporation
Paul M. Brent

By /s/ Paul M. Brent
Paul M. Brent
Attorneys for the Plaintiffs, Dove Audio, Inc., Michael Viner and Jerry Leider

PROOF OF SERVICE

(U.S. Bankruptcy Court, Central District, Local Rule 105(3))

I am employed by the law firm of Danning, Gill, Diamond & Kollitz, LLP in the County of Los Angeles, State of California. I am over the age of 18 and not a party to the within action. My business address is 2029 Century Park East, Suite 1900, Los Angeles, California 90067-3005

On this date I caused to be served the **FOURTH AMENDED COMPLAINT TO AVOID FRAUDULENT TRANSFERS AND TO RECOVER GENERAL AND PUNITIVE DAMAGES** on all interested parties as follows:

SEE ATTACHED SERVICE LIST

✓✓ (By Mail) I caused each envelope, with postage prepaid, to be placed in the United States mail at Los Angeles, California.

_____ (By hand) I caused each envelope to be delivered by hand.

_____ (By Overnight Courier) I caused each envelope, with postage prepaid, to be sent by Federal Express/Express Mail.

_____ (By Facsimile Transmission) I caused each page of the document to be sent by automatic facsimile transmission to the following telephone numbers: (_ _ _) _____ - _____ and confirmed by voice communication that the transmission was received.

_____ (State) I declare under penalty of perjury under the laws of the State of California that the above is true and correct.

✓✓ (Federal) I declare that I am employed in the office of a member of the bar of this Court at whose direction the service was made.

I declare under penalty of perjury that the foregoing is true and correct. Executed at Los Angeles, California on February 12, 1997.

/s/ Debbie Throckmorton
DEBBIE THROCKMORTON

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Supreme Court, U.S.
FILED
JAN 20 2004
OFFICE OF THE CLERK

No. 03-891

IN THE

Supreme Court of the United States

DAVID A. GILL, Chapter 7 Trustee,

Petitioner,

v.

STEVEN H. STERN, Individually, and as Trustee of the Steven H. Stern, Inc. Profit Sharing Plan,

Respondents.

ON PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE NINTH CIRCUIT

BRIEF IN OPPOSITION

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TABLE OF CONTENTS

	Page
Table of Cited Authorities	ii
Reasons for Denying the Petition	1
Statement of Case	2
A. Material Background and Circumstances.	2
B. Proceedings Below.	4
Argument	5
A. Fraudulent Transfer Laws and Exemption Laws Address Entirely Different Circumstances.	5
B. There is No Circuit Split Over the Issues Decided Here.	6
C. No Compelling Federal Interest is At Stake in Exemption Planning Cases.	10
Conclusion	11

TABLE OF CITED AUTHORITIES

Page

Cases:

Forsberg v. Security State Bank, 15 F.2d 499 (8th Cir. 1926) 6-7

In re Arro, 170 F.3d 934 (9th Cir. 1999) 10

In re Ginther, 282 B.R. 16 (Bankr. D. Kan. 2002) ... 10

In re Sholdan, 217 F.3d 1006 (8th Cir. 2000) ... 1, 6, 7, 8, 9

In re Stern, 345 F.3d 1036 (9th Cir. 2003) 1, 7, 9

Kangas v. Robie, 264 F.2d 92 (8th Cir. 1920) 6

Patterson v. Shumate, 504 U.S. 753, 112 S. Ct. 2242, 119 L. Ed. 2d 519 (1992) 10, 11

Tavenner v. Smoot, 257 F.3d 401 (4th Cir. 2001) .. 9

Wudrick v. Clements, 451 F.2d 988 (9th Cir. 1971) 1, 7

Rules:

U.S. Sup. Ct. R. 10 1

U.S. Sup. Ct. R. 10(c) 10

REASONS FOR DENYING THE PETITION

While it is true that this case presents a question about "the intersection of fraudulent transfer law and exemption planning", Petition for Certiorari at *i*, it is *not* true that a circuit split exists over the question presented here. Morever, even if there are differing results among the circuits, certiorari is not warranted because the underlying question relates exclusively to the operation of different states' exemption laws. No federal question of pervasive national importance exists that this Court could resolve on a common plane.

A. There is no "split" because both the Eighth and Ninth Circuits allow a bankruptcy court to take into account evidence of fraud that is extrinsic to the successful conversion of non-exempt assets into exempt assets. *Compare In re Sholdan*, 217 F.3d 1006, 1010-11 (8th Cir. 2000) ("there was ample evidence extrinsic to the mere conversion of assets") with *In re Stern*, 345 F.3d 1036, 1044 (9th Cir. 2003), where the Ninth Circuit quotes from its earlier decision in *Wudrick v. Clements*, 451 F.2d 988 (9th Cir. 1971), which recognized that "[a] different case would be presented if on the eve of bankruptcy [to create exempt assets] a debt were created with no intention of repaying the creditor, either by purchasing goods on credit or borrowing money without security." *Wudrick*, 451 F.2d at 990.

Petitioner's problem is not that the circuits conflict, but that the trustee in *Sholdan* was able to tender evidence of extrinsic fraud that was sufficient to nullify the exemption, while Petitioner could not meet his burden here, even to show a triable issue. This does not amount to a split in the circuits. Rule 10 of the Rules of the Supreme Court.

B. Moreover, the legal "intersection" Petitioner writes about is decidedly local in flavor. While Petitioner seeks to draw the Court's attention with liberal references to ERISA, in fact, the fraudulent transfer law Petitioner invoked was the California UFTA and the exemption scheme asserted by Respondent is part of the California Enforcement of Judgments Law. Indeed, in the *Statutes Invoked* section of his Petition, Petitioner refers only to the California Civil Code (the California UFTA) and the California Code of Civil Procedure (the California Enforcement of Judgments Law). No other circuit has addressed how these California statutes operate in concert with each other, so the circuits cannot be "split" over the question raised here. Neither are federal questions or issues of national importance raised by how two California statutes interact.

The most favorable characterization of the circumstances Petitioner could claim is that the Eighth Circuit has decided that "filling up" Minnesota exemption categories on the eve of a bankruptcy filing could be fraudulent, while the Ninth Circuit decided that "filling up" California exemption categories on the eve of a state law levy cannot be fraudulent. But since the underlying exemption schemes are different, and were established by different legislatures to reflect different — and local — legislative dynamics and values, there is no pervasive, national and uniform plane upon which this Court can address, much less resolve, the questions Petitioner raises.

STATEMENT OF CASE

A. *Material Background and Circumstances.*

While Petitioner provides a colorful — and one-sided — history in the *Fraudulent Transfer* section of his Petition (pp. 4-7), it is clear that most of this "background" is designed

primarily to curry visceral sentiment against Respondent because it is irrelevant to the legal issue Petitioner himself presents. That is, allegations that Stern fraudulently transferred certain assets to third persons are not relevant to analyzing whether Stern's decision to convert into exempt form *other* assets he owned — and continues to own — is "fraudulent" such that the state law exemption scheme should be unavailable to Stern.[1] Those allegations about fraudulent transfers allegedly made to third persons are equally irrelevant to the question whether the retention of assets by Stern after they were converted to exempt form is somehow a fraudulent *transfer*.

What *is* relevant is that beginning in 1974, Steven H. Stern began saving for his retirement and while he used a variety of investment vehicles for that purpose, he always maintained his interest in the same Retirement Assets, never transferring the Retirement Assets to anyone else. Indeed, other than market fluctuations, the corpus of the Retirement Assets has not materially changed since 1989.

As time passed, Congress and the California Legislature established or sanctioned different investment vehicles and Respondent "rolled" his Retirement Assets from one vehicle to another as the applicable laws and pertinent circumstances evolved. Prior to 1992, Stern rolled over the Retirement Assets into an Individual Retirement Account ("IRA") when the corporate sponsor of a prior corporate plan dissolved in 1989. In 1992, three years before he filed his bankruptcy case, Stern again rolled over his Retirement Assets, this time back into a corporate retirement plan (the "1992 Rollover").

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1. Indeed, allegations that Stern fraudulently transferred assets to a third-party were alleged in separate claims not at issue in the underlying summary judgment motion and have now been dismissed by the Petitioner.

Stern filed his bankruptcy petition in August 1995 and claimed his interest in the Retirement Assets exempt from the bankruptcy trustee's administration.[2]

B. ***Proceedings Below.***

Petitioner sued to recover the Retirement Assets on a fraudulent transfer theory.[3] He also separately objected to Stern's claim of exemption of the Retirement Assets. Petitioner claims the 1992 Rollover is a fraud because the 1992 Rollover occurred soon after a state court judgment was entered against Stern on an arbitration award, but since it was undisputed that in the corporate retirement vehicle the Retirement Assets met the standards and limitations on the state law exemption, the most this proved was the purposeful conversion of assets into exempt form. Moreover, there existed the equally undisputed fact that other, surrounding circumstances had further evolved, such that use of a corporate business structure and associated retirement vehicle had again become advisable. Thus, Petitioner produced no *extrinsic* evidence of fraud pertinent to the assets claimed to be exempt.

Despite the fact that there is no direct evidence on point in the record, and despite the presence of evidence tending to prove the 1992 Rollover was motivated by the coincidence of evolving business circumstances, Stern repeatedly agreed that

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2. Stern alternatively argued that the Retirement Assets were excluded from the bankruptcy estate. Petitioner prevailed on this issue before the Ninth Circuit and it is the subject of a Conditional Cross-Petition for Certiorari.

3. Notably, Petitioner sued the third party transferees over the first group of assets, but never proved they were fraudulent transfers either.

the courts below could assume the 1992 Rollover was motivated, at least in material part, by his desire to be sure he could shield from creditors' hands the most that the California exemption law would allow. Stern prevailed in proceedings before the bankruptcy court, the district court and the Ninth Circuit.

The courts below held that it is not "fraudulent" to do what the law contemplates. That is, it is not fraudulent for one who suffers a judgment to read, think about and take advantage of laws that exempt identified assets from the seizure rights of a levying judgment creditor. And although the courts did not deploy this reasoning, neither was there a transfer of the assets claimed to be exempt, since Stern owned the same Retirement Assets before the 1992 Rollover that he owned after the 1992 Rollover. Since there was no "transfer", and there was nothing "fraudulent" about the 1992 Rollover, the courts below were quite correct to dismiss the Trustee's fraudulent transfer lawsuit. No circuit split resulted and no federal question arose.

ARGUMENT

A. *Fraudulent Transfer Laws and Exemption Laws Address Entirely Different Circumstances.*

Fraudulent transfers are *conveyances* by a debtor (or debtor-to-be) by which she divests herself of ownership of a thing but typically retains *de facto* influence and control over it. Or, she has gotten nothing for it. Either way, it is the *hypothecation* out of a debtor's estate, so that the thing is not amenable to levy, that triggers fraudulent *transfer* scrutiny. Likewise, the defendant in a fraudulent transfer action is not the judgment debtor, but a third person who received assets from the judgment debtor and who might be ordered to return them — not to the judgment debtor, but to his creditors.

Exemptions are different. Exemption rights operate only with respect to assets *still owned by a debtor* on the Scrutiny Date (typically, the date of a bankruptcy petition or a judgment creditor's levy). That is, the asset in question is owned by a debtor and thus amenable to levy, but debtor protection laws insulate it from forced sale. Thus, in contrast to a fraudulent transfer lawsuit, in exemption litigation, the defendant (respondent) is the judgment debtor himself. It follows that what Petitioner caustically describes as "exemption planning", does not involve a *transfer by the debtor* at all. Rather, it involves planning as to how a person is best advised to hold the property he owned and continues to own.[4]

B. *There is No Circuit Split Over the Issues Decided Here.*

The legal intersection Petitioner writes about is not normally controversial because "filling up" exemption categories is recognized to be different from fraudulent transfers. Indeed, it simply makes no sense for a debtor's creditors to concern themselves with purportedly fraudulent transfers *to* their judgment debtor. The Eighth Circuit in *Sholdan* acknowledges that a debtor is allowed "to convert non-exempt assets into exempt property for the express purpose of holding it as a homestead and thereby putting the property beyond the reach of creditors", 217 F.3d at 1011, *citing Kangas v. Robie*, 264 F.2d 92, 93-94 (8th Cir. 1920). *Accord*, *Forsberg v. Security State Bank*, 15 F.2d 499,

4. In some "exemption planning" situations, non-exempt property is traded for exempt property, or is liquidated so the proceeds can be used to buy exempt property. Either way, even though there are nominal transfers, the total value of the debtor's estate remains essentially the same. This case presents an even narrower version of "exemption planning", one where the *same assets* are owned before and after the Scrutiny Date, and only the ownership vehicle or framework is slightly different.

501 (8th Cir. 1926). Similarly, the Ninth Circuit has stated, twice, " 'that the purposeful conversion of nonexempt assets to exempt assets on the eve of bankruptcy is not fraudulent per se.' " *Stern*, 345 F.3d at 1043, quoting *Wudrick*, 451 F.2d at 989.

The concepts are in tension only where the assets claimed as exempt are affected by facts assertedly establishing a fraud that goes materially beyond the creation of exempt assets (or the conversion of non-exempt assets into exempt assets).[5] Although varying fact patterns may cause tension between these concepts, this tension does not mean the circuits are "split" for purposes of certiorari to this Court.

In *Sholdan*, a 90 year old Minnesotan cashed out some savings deposits, sold payment rights and bought a $135,000 house he claimed exempt as a homestead. The trustee attacked the exemption and the *Sholdan* court held that there existed sufficient facts, extrinsic to the alleged creation of an exempt asset, to establish actionable intent to defraud such that Mr. Sholdan lost his right to *Minnesota* exemptions. From this, Petitioner concludes that Mr. Stern should have lost his right to *California* exemptions.

That Petitioner did not achieve his desired goal is not due to a split in the circuits' legal reasoning but rather to the fact that Petitioner's evidence was simply not as strong as the trustee's evidence in *Sholdan*. Indeed, in *this* case, Petitioner had *no* such evidence. In this case, the bankruptcy court repeatedly asked Petitioner's counsel to explain what facts he would show at trial, *apart from the purposeful and successful conversion*

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5. But even here, the fraudulent *transfer* theory petitioner advanced could not be viable because Stern never *transferred* anything.

of non-exempt assets into exempt assets. Petitioner could never answer the court's question, other than to point to surrounding circumstances, *i.e.*, transactions he claimed showed there were fraudulent transfers *to third parties*. But evidence of what Stern did with Asset Group A is not relevant to whether Asset Group B is exempt.[6] The extrinsic evidence Petitioner needed to adduce, but could not, had to pertain to the assets he claimed as exempt, not some other assets. Petitioner never offered evidence of extrinsic fraud relating to the assets Stern claimed as exempt.

In contrast, the trustee in *Sholdan* had more to show, namely that Mr. Sholdan did not intend to reside in the "homestead". This extrinsic fact directly affected the asset claimed to be exempt and went far beyond the mere purposeful conversion of non-exempt assets into *exempt* assets. Indeed, this extrinsic fact *negated* the creation of exempt assets and the whole point in *Sholdan* was that *no exempt asset was actually created*, while Mr. Sholdan presented a charade that it was. In the words of the Eighth Circuit,

> [i]t is one thing to convert non-exempt assets into exempt assets for the express purpose of holding it as a homestead and thereby putting the property beyond the reach of creditors. However, it is quite another thing to acquire title to a house for no other reason than to defraud creditors.

217 F.3d at 1011. That is, acquiring title to a house is not the same thing as establishing a homestead and only a homestead is exempt. *This* fraud, quite different from successful creation of an exempt asset, defeated Mr. Sholdan's claimed exemption.

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6. Moreover, Petitioner did not ever prove the third-party allegations. Please see footnotes 1 and 3.

Thus, *Sholdan* does not endorse a trustee's use of fraudulent transfer law to take exempt property from a debtor, or to negate an exemption otherwise established under non-bankruptcy law. Indeed, in *Sholdan*, while the Eighth Circuit discussed Mr. Sholdan's intent to defraud, it never identified anything that Mr. Sholdan transferred, so it cannot be said that the *Sholdan* court relied on fraudulent transfers to void an exemption. Yet that is exactly what Petitioner tried to do here, so *Sholdan* is not "split" from the case Petitioner presented.

In short, *Sholdan* is a case where the debtor failed to establish the facts needed to create a *Minnesota* exemption. *Stern* is a case where the debtor *succeeded* in establishing the facts needed to create a *California* exemption. This difference in outcomes, on these questions, hardly establishes a "split" in the circuits.

Petitioner's other citation, *Tavenner v. Smoot*, 257 F.3d 401 (4th Cir. 2001), is even more readily distinguished from *Stern*. In *Tavenner*, the debtor made actual transfers of money to pay "wages" to, and buy a home for, his son; to buy cars for other relatives; and other such mischief. 257 F.3d at 405. This was a true fraudulent transfer environment, so it is different from both *Sholdan* and this case, and the issue was whether the transfers were voidable where the asset would have been exempt, had the transfers not yet been made when the Scrutiny Date arrived. 257 F.3d at 405-06.

Tavenner is thus different from both *Stern* and *Sholdan* in that the debtor hypotheticated assets and *then* claimed them exempt (although it is like *Sholdan* in that the exemption failed for lack of a threshold showing). That is, in *Tavenner*, the transfer defeated the exemption; whether it was *fraudulent* or not really was irrelevant. It follows that *Tavenner* and *Stern* do not create

a split in the circuits because they address different facts and different legal issues.

C. *No Compelling Federal Interest is At Stake in Exemption Planning Cases.*

Since it is clear that the three circuit-level decisions cited by Petitioner in fact create no cognizable "split", certiorari is not warranted unless a compelling federal interest has been put in play. Rule 10(c) of the Rules of Supreme Court. No such circumstance exists here.

How the several states, and bankruptcy courts sitting in them, interpret and apply their own state exemption laws is a peculiarly local issue. *In re Arro*, 170 F.3d 934, 935-36 (9th Cir. 1999) (debtor entitled to assert state law exemptions if the state where the bankruptcy petition has been properly filed has not "opted out" of the federal exemption scheme); *In re Ginther*, 282 B.R. 16, 20 (Bankr. D. Kan. 2002) ("exemption laws are local and 'pertain to the remedy having no extraterritorial effect.' ") Exemption laws vary greatly, properly so.[7] It would be nearly meaningless for this Court to attempt to decide what is and is not permissible "exemption planning" on a blanket basis when there are no blanket exemption laws for the pronouncement to apply to.

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7. The Bankruptcy Code recognizes that each state decides what exemptions are allowable in its own courts, and also authorizes the states to decide what exemptions can be claimed by bankruptcy debtors resident in the state. This is one of the only areas where rights to property in bankruptcy cases is left to state-to-state decisions. *See Patterson v. Shumate*, 504 U.S. 753, 758, 112 S. Ct. 2242, 2246, 119 L. Ed. 2d 519 (1992) (when it desired to do so, Congress has restricted the scope of applicable law to "state law").

CONCLUSION

It cannot be "fraudulent" for someone who has suffered a money judgment under state law to do what state law debtor protection statutes specifically contemplate. *No* circuit has held that where all that occurs is that exempt assets are successfully created from assets that not have been exempt, exemption rights are lost. There certainly can be no "split" where the circuits do not disagree on the underlying principle.

Likewise, the circuits are in agreement that *extrinsic* evidence of fraud, that goes *beyond* the mere creation of exempt property, could negate a debtor's right to an exemption. The difference between this case and the citations with which Petitioner tries to contrast it is that he had no evidence on the issue. This is not cause for certiorari to this Court. There being no federal rights, obligations or remedies put in issue by Petitioner,[8] certiorari should be denied.

Respectfully submitted,

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8. Not incidentally, a federal issue *does* exist in this case, but it arises only in connection with Respondent's Cross-Petition. Petitioner prevailed below on his argument that the Retirement Assets in question were not *excluded* from the bankruptcy estate under ERISA and *Patterson v. Shumate*. Hence Respondent can and does raise a federal issue but Petitioner does not.

(3)

No. 03-891

Supreme Court, U.S.
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In The
Supreme Court of the United States

DAVID A. GILL, CHAPTER 7 TRUSTEE,

Petitioner,

v.

STEVEN H. STERN,

Respondent.

On Petition For A Writ Of Certiorari To The United States Court Of Appeals For The Ninth Circuit

REPLY BRIEF

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TABLE OF CONTENTS

Page

INTRODUCTION 1

ARGUMENT 1

CONCLUSION 5

TABLE OF AUTHORITIES

Page

CASES

In re Sholdan, 217 F.3d 1006 (8th Cir. 2000)..... 1, 2, 3, 4, 5

Tavenner v. Smoot 257 F.3d 401 (4th Cir., 2001), cert. denied, 534 U.S. 1116 (2002)..... 2, 4, 5

STATUTES

11 U.S.C. § 548 4

INTRODUCTION

By his Brief in Opposition ("Brief"), Respondent Steven H. Stern ("Stern") urges this Court to deny the Petition for Writ of Certiorari ("Petition"), asserting that there is no circuit split and there is no question of "pervasive national importance," Brief at page 1, for this Court to resolve. Stern argues that at most what is involved is the interpretation of different state exemption laws, Brief at pages 1-2.

Petitioner, David A. Gill, Chapter 7 Trustee ("Trustee") urges this Court to grant the Petition. The split among the circuits has been made apparent by the Ninth Circuit Court of Appeals' Amended Opinion below. The fact that different state exemption laws are involved is not germane to the split, and the question presented in this case as to the "intersection of fraudulent transfer law and exemption planning," Brief at page 1, Petition at page i, is the height of importance and deals with the interpretation of the Bankruptcy Code.[1]

ARGUMENT

The Petition is premised upon the split among the circuits created by the Ninth Circuit's Amended Opinion below as contrasted with the decision by the Eighth Circuit Court of Appeals in *In re Sholdan*, 217 F.3d 1006 (8th Cir. 2000) and by the Fourth Circuit Court of Appeals

[1] The Trustee will separately file a Brief in Opposition to the "Conditional Cross-Petition for Writ of Certiorari" (03-1055) filed concurrently by Stern with his Brief in Opposition.

in *Tavenner v. Smoot*, 257 F.3d 401 (4th Cir. 2001), cert. denied, 534 U.S. 1116 (2002). The facts in this case are set forth in the Petition and although Stern characterizes the Trustee's statement of facts as " . . . a colorful – and one-sided – history . . . " designed to " . . . curry visceral sentiment . . . ," Brief at pages 2 to 3, Stern does not point to any particular fact or facts that the Trustee has misstated. Stern's Brief thus turns on his assertions that there is no split among the circuits or nothing of importance for this Court to address.

It is in fact clear that the majority opinion by the Ninth Circuit below creates an ironclad rule that forecloses an analysis of extrinsic facts in determining when exemption planning has passed over into fraudulent transfer. In contrast to the Ninth Circuit, *Sholdan* and *Tavenner* require a factual analysis and hold that a sufficient factual showing can be made that a transfer has gone beyond exemption planning into a fraudulent transfer. What the Ninth Circuit has decided cannot be tried, the Eighth and Fourth Circuits have decided must be tried. An analysis of the Eighth and Fourth Circuit cases shows the difference.

In the case of *In re Sholdan*, 217 F.3d 1006 (8th Cir. 2000), the Eighth Circuit was faced with an appeal from the affirmance of a bankruptcy court order that sustained the bankruptcy Trustee's objection to the debtor's homestead exemption. The debtor, when 90 years of age and afflicted with various medical problems and living in an assisted care facility, had liquidated almost all of his non-exempt property and converted it into exempt property in the form of a house. Shortly thereafter, the debtor filed bankruptcy and then passed away. *In re Sholdan*, *supra*, at page 1008. The matter had previously been before the

Eighth Circuit, when the Circuit ruled that the facts did not support the Bankruptcy Court's finding that the debtor had acted with the "intent to hinder or delay" but remanded for consideration of whether the facts supported a finding that the debtor had acted with the "intent to defraud." *In re Sholdan*, *supra*, at page 1008. The Bankruptcy Court on remand found that such intent underlay the conversion from non-exempt property to exempt property, and was affirmed by the District Court and then by the Eighth Circuit, *Sholdan*, *supra*, at page 1008-1009. Nothing in the *Sholdan* court's discussion of the Minnesota version of the Uniform Fraudulent Transfer Act is of consequence to the decision. The Eighth Circuit focused on bankruptcy issues related to transfer of assets. The precise provisions of the state exemption statutes do not come into play. Rather, the decision turns on weighing the facts, evaluating the circumstantial evidence adduced to determine the question of transferor intent. The Bankruptcy Court noted a "radical departure" from the debtor's prior lifestyle in the transfers under examination. Based on the record before it, the Eighth Circuit affirmed, stating " . . . we find the bankruptcy court correctly concluded there was ample evidence extrinsic to the mere conversion of assets that shows fraudulent intent on the part of the debtor. It is one thing to convert non-exempt assets into exempt property for the express purpose of holding it as a homestead and thereby putting the property beyond the reach of creditors. [citation]. However, it is quite another thing to acquire title to a house for no other reason than to defraud creditors." *Sholdan*, *supra*, at 1010-1011.

The facts here demonstrate a no less radical departure in Stern's lifestyle. In the context of making the IRA Transfer, Stern also obtained a divorce and made other

surrounding transfers. This is surely no less a radical change than the *Sholdan* change. But, in contrast to *Sholdan*, the Ninth Circuit has ruled that on these facts, no trial is required.

Similarly, in *Tavenner v. Smoot*, 257 F.3d 401 (4th Cir. 2001), cert. denied, 534 U.S. 1116 (2002), the issue before the Fourth Circuit was " . . . whether a bankruptcy trustee can avoid a transfer of potentially exempt property on the ground that a debtor transferred the property with the intent to hinder, delay, or defraud his creditors under 11 U.S.C. § 548." *Tavenner*, *supra*, at page 404. That is the precise issue that was before the Ninth Circuit below. The circuits, however, resolved the matter differently. The Ninth Circuit concluded that the matter could be resolved as a question of law. The Fourth Circuit resolved the matter as a factual issue after a hearing, *Tavenner*, *supra*, at pages 405-406. Here, again, as in *Sholdan*, the peculiarities of any state law were not germane. Rather, the Fourth Circuit concluded, first, that " . . . transfers of exemptible property *are* amenable to avoidance and recovery actions by bankruptcy trustees . . . " [emphasis in original], *Tavenner*, *supra*, page 406, and then went on to conclude that " . . . the evidence amply supports the bankruptcy court's finding that Smoot transferred the FELA proceeds to Glass Apple with the intent to hinder, delay, or defraud his creditors." *Tavenner*, *supra*, at page 408. The Bankruptcy Court also found that the transfer was constructively fraudulent, *Tavenner*, *supra*, at page 408, and was affirmed as well. Here, again, the contrast with Stern is stark. It is the difference between determination of an issue as a matter of law and only after a full evidentiary hearing.

Nothing in either *Sholdan* or *Tavenner* deals with the peculiarities of specific state exemption laws. This case does boil down to a conflict among the circuits in the approach to the intersection of fraudulent transfer law and exemption planning. Deprived of the cover that all that exists here is a divergence of interpretation of differing state exemption laws, Stern does not argue, nor can he argue, that the issue of when exemption planning becomes fraudulent transfer, which has bedeviled the courts, trustees, and counsel, is not of national importance.

CONCLUSION

For all the reasons set forth herein and in the Petition for Writ of Certiorari, it is respectfully requested that the Petition be granted.

Respectfully submitted,

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